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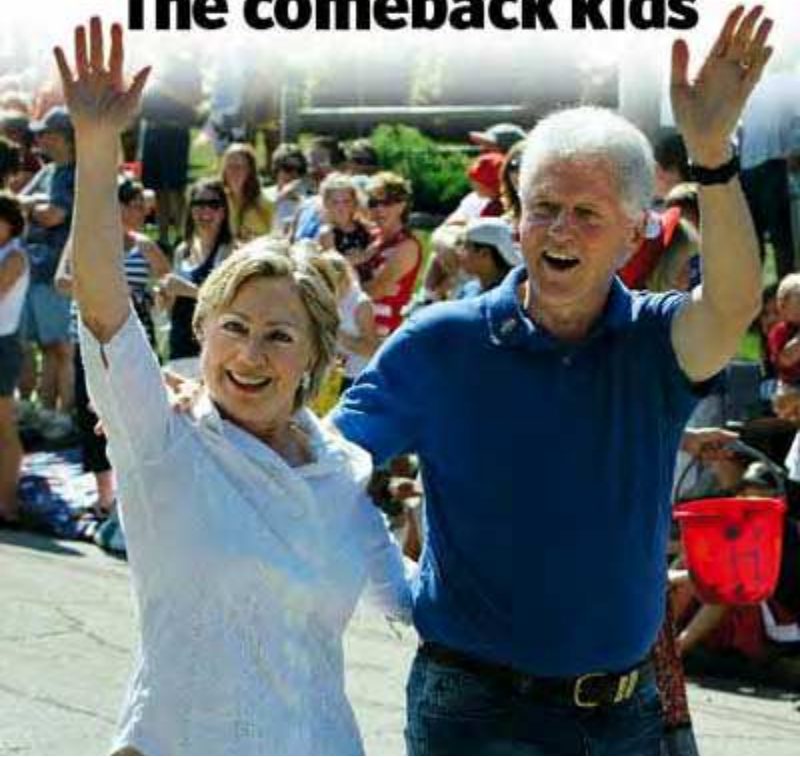
The comeback kids



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Print Edition October 6th 2007

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The American presidency is Hillary Clinton's to lose. But that doesn't make her a shoo-in just yet: leader

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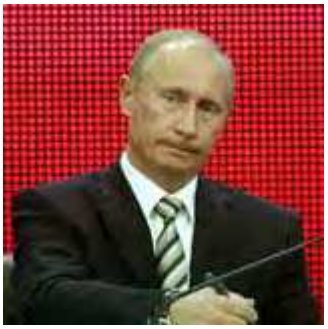
Politics this week

Oct 4th 2007
From The Economist print edition

EPA



Russia's president, Vladimir Putin, announced that he would head the United Russia ticket in December's general election and hinted that he might then become prime minister. That seemed a neat answer to his desire to remain in power after he has to step down as president at the end of his second term of office in March 2008. See article

Ukraine's election produced an inconclusive result. But a strong performance by Yulia Tymoshenko's party seemed likely to lead to her returning as prime minister of a new orange coalition, like the one she briefly led in 2005. See article

The **Italian government** agreed a budget for 2008 that slashes corporate taxes but leaves public spending largely untouched. Nevertheless the finance ministry predicted a lower budget deficit, thanks mainly to higher revenues from people who had previously not paid taxes. See article

The **king of Spain**, Juan Carlos, defended the monarchy as a pillar of Spain's democratic constitution. Recently nationalists in Catalonia had been questioning the king's value.

Giving quarter

Figures submitted to America's Federal Elections Commission showed that in the third quarter of the year Hillary Clinton overtook her nearest rival, Barack Obama, after falling behind him in **fund-raising** efforts in the first six months. A *Washington Post* poll showed her ahead of him by 33 points in the race for the Democratic nomination. See article

President George Bush vetoed a proposal, passed by both chambers of Congress, to expand funding for **children's health insurance** by $35 billion a year. The Democratic speaker of the House of Representatives, Nancy Pelosi, accused him of wielding a “cruel veto pen” and promised a “vigorous fight” but the Democrats lack the votes to overturn him. See article

The American army lost fewer troops in **Iraq** in September than it has for more than a year. Only 42 died in combat, and another 21 died from non-hostile causes. Attacks on civilians were down too. See article

The administration also hailed some success in the war on **drugs** in America. Cocaine prices were said to have doubled, after a crack-down on smuggling.

Stemming the saffron tide

The junta ruling **Myanmar** was the butt of criticism from most of the world after its bloody suppression of nearly two weeks of pro-democracy protests led by monks. It reported that ten people had died. Diplomats put the toll many times higher. Ibrahim Gambari, the United Nations' special envoy, visited the country and met both the junta's leaders and Aung San Suu Kyi, the detained opposition leader, in an effort to restart a dialogue. See article

Getty Images

Kim Jong Il, North Korea's dictator, met South Korea's president, Roh Moo-hyun, for the second-ever **inter-Korean summit**. The two men agreed to seek a formal end to the civil war of the 1950s. Meanwhile, Chinese officials reported that North Korea has agreed to disable its main nuclear reactor and give full details of its nuclear programme by the end of the year. See article

In **Pakistan** General Pervez Musharraf proceeded with plans to have himself re-elected for another term as president. Many opposition members resigned in protest, arguing that he should not be re-elected while still head of the army, and that general elections should be held before the presidential vote. General Musharraf has appointed the country's head of intelligence to replace him as army chief, a job he has said he will give up before being sworn in next month. See article

Fourteen people have been arrested in connection with a bombing in Male, capital of **the Maldives**, which injured 12 tourists. The Maldives has seen political unrest in recent years in protest at the 29-year rule of President Maumoon Abdul Gayoom. This is the first bombing on the islands.

More than 40 people, mostly local soldiers and policemen, were killed in two suicide-bombings in the Afghan capital, **Kabul**. The Taliban claimed responsibility.

Trade winds

Eighteen months after negotiations were concluded, the White House sent a bill to Congress to ratify a **free-trade agreement** with Peru. The agreement now incorporates stiffer provisions on labour rights and the environment, inserted at the insistence of the Democrats. See article

In **Costa Rica** tens of thousands demonstrated against ratification of a free-trade agreement with the United States ahead of a referendum on the issue on October 7th.

Supporters and allies of **Ecuador's** socialist president, Rafael Correa, appeared to have gained a clear majority in an election for a Constituent Assembly. Mr Correa said he plans to dissolve the country's Congress, dominated by his opponents. See article

Let's solve it, some time

Israel's prime minister, Ehud Olmert, and the **Palestinian** president, Mahmoud Abbas, agreed to start formal negotiations on Palestinian statehood after an American-sponsored conference expected next month. But Mr Olmert said no to Mr Abbas's demand for a timetable for agreeing on borders, including Jerusalem's, and dealing with the future of the Palestinian refugees.

France's foreign minister, Bernard Kouchner, urged the European Union to take the lead by tightening and widening financial sanctions against **Iran** because, he said, the world could not bank on UN pressure to stop Iran making a nuclear bomb. See article

An African Union contingent of mainly Nigerian peacekeepers was attacked by unknown assailants (perhaps a splinter group of one of the three main rebel factions) in the embattled western Sudanese province of **Darfur**, leaving at least ten dead. The incident may hobble peace talks in Libya later this month.

AFP

Meanwhile, tension rose between the **Sudanese** government in Khartoum and former rebels in the south of the country, where a separate peace deal was signed two years ago.

A rescue got under way after more than 3,000 miners were trapped underground in **South Africa**.

Fighting broke out over territory between Somaliland, the de facto independent northern bit of **Somalia**, and Puntland, a semi-autonomous entity in the north-east. The southern part of the country remained as edgy as before. See article

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Business this week

Oct 4th 2007
From The Economist print edition

Stockmarkets surged around the world on hopes that the worst of the credit crisis was over and expectations that the Federal Reserve would ride to the rescue if not. In America the Dow Jones Industrial Average briefly reached a record high. A raft of Asian markets climbed new peaks as well. See article

Banking shares rose despite **profit warnings** from a number of big banks. Citigroup said that its earnings would be hit by write-downs on leveraged loans and mortgage-backed securities, as well as by charges in its consumer business. UBS, a Swiss bank, said that it would report a loss for the quarter. Credit Suisse and Deutsche Bank also owned up to big write-downs caused by this summer's seizing up of credit markets. See article

Citigroup's troubles did not stop the American bank from agreeing to take full control of **Nikko Cordial**, a Japanese broker. The acquisition is designed to position Citigroup for an expected switch by Japanese household savers into higher-yielding assets.

Loonie lift

Helped by the strength of the Canadian dollar, **Toronto-Dominion Bank** agreed to buy **Commerce Bancorp**, an American retail bank, for $8.5 billion. The deal cements the Canadian bank's presence in America's north-east.

The carousel of **stock exchange deals** continued to whirl. America's NASDAQ agreed to acquire the Boston Stock Exchange for $61m. NASDAQ faces greater competition in its pursuit, in partnership with Borse Dubai, of OMX, a Nordic exchange operator. The Qatar Investment Authority applied to increase its stake in OMX, raising the chances of a bidding war.

Nokia, a mobile-handset maker, acquired Navteq, a **digital-mapping** company, for a pricey $8.1 billion. Navteq's software is used on satellite-navigation devices and websites, among other things. Nokia is betting that location-based services will become increasingly popular among mobile-phone users. See article

Skype hyped

EBay, an internet auctioneer, admitted that it had paid too much for Skype, an internet phone service that it acquired for $2.6 billion in 2005. EBay announced that it would take an **impairment charge** of $900m in the light of Skype's disappointing performance. See article

The European Commission reaffirmed its decision to allow a 2004 merger between the music divisions of **Sony** and **Bertelsmann**. Independent record labels had forced a review on competition grounds and may appeal again.

France's stock-market regulator sent a report to the public prosecutor's office naming 21 key figures at **Airbus** and its parent, EADS, in relation to possible insider-trading offences. The regulator has been investigating how much executives knew about manufacturing problems that were to delay the delivery of the A380 superjumbo before they sold shares or exercised stock options. When difficulties with the giant plane's wiring system became public in June 2006, EADS lost 26% of its value in one day.

In a busy week for **British broadcasters**, antitrust authorities ruled that BSkyB's acquisition of a minority stake in ITV, the country's leading terrestrial commercial broadcaster, restricted competition. No such worries at the publicly funded BBC, whose commercial arm snapped up a 75% stake in Lonely Planet, a travel publisher.

Anglo American, a mining giant, continued to reduce its stake in AngloGold Ashanti. A share placement

will take Anglo American's holding in the company down to 17.3%, in line with its strategy of shifting its focus away from gold towards other commodities such as platinum, diamonds, coal and iron ore. See article

China formally launched its **sovereign-wealth fund**. The fund, which has roughly $200 billion under management, has earmarked one-third of that money to acquire the investment arm of the central bank. The fund has also bought a stake in Blackstone, a private-equity firm.

As expected, **Dominique Strauss-Kahn**, a former French finance minister, was selected to be the next head of the International Monetary Fund. Mr Strauss-Kahn will take up the post in November. See article

Dipping dollar

The **dollar** touched new lows against the euro, as more evidence emerged of weakness in the American economy. The number of signed contracts to buy existing homes fell again in August and a monthly survey by the Institute of Supply Management indicated softness in the services sector. European politicians meanwhile expressed concern about the impact of the euro's rise on exports. Inflation in the currency zone rose to 2.1% in September, despite the euro's strength.

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KAL's cartoon

Oct 4th 2007
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Illustration by Kevin Kallaugher

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American politics

The comeback kids

Oct 4th 2007
From The Economist print edition

The American presidency is Hillary Clinton's to lose. But that doesn't make her a shoo-in just yet

AP

IF GREAT writers have a special insight into the souls of their countrymen, Hillary Clinton ought to be pleased. Philip Roth, one of the grandest old men of American letters, said last year that if anyone could lose 50 states for the Democrats, she could. This week he said he is no longer sure.

Mr Roth is hardly alone, either in his previous hatred for the former first lady or in his grudging new acceptance of her. It is still more than three months until the votes are cast in the first primaries, and over a year until the election. With no incumbent president or vice-president running, this should be the most open race for 80 years—but it certainly doesn't feel that way. Never mind the oddness, in a republic, of having Bushes and Clintons in charge for, possibly, 28 years on the trot: at the moment, the return of Hillary and Bill Clinton to the White House looks likelier than any alternative (see article).

Mrs Clinton is polling an average of some 18 points clear of her nearest rival, Barack Obama, for the Democratic nomination, and one poll this week put her 33 points ahead. She leads solidly in all the early primary states except, crucially, Iowa (which matters because it comes first), where she has only an insignificant lead. In head-to-head polls, she now handily defeats any of her Republican rivals—and the Republicans are divided and demoralised. And this week she reversed the only measure on which she was trailing: in the third quarter of the year, she narrowly beat Mr Obama in raising campaign contributions. Mr Obama's superior fund-raising has been the main source of worry for the Clintonistas.

That does not mean she will win. Things could go wrong even in the primaries: ask Howard Dean, who seemed unstoppable for the Democratic ticket at Christmas 2003, before it all went wrong one night in Des Moines. There are plenty of things that could trip up Mrs Clinton, not least her husband. But barring some stumble or scandal, Americans will as usual decide on the candidates' merits, so the key to the election is to decide which qualities are most in demand this time around.

Brilliantly dull

Top of the list surely must come competence—the attribute that has been most sorely lacking in the Bush administration, whether in the planning for post-war Iraq, the response to Hurricane Katrina or the management of the federal budget, which George Bush, like a reverse King Midas, has transmuted from a $240 billion surplus to a $160 billion deficit.

This is where Mrs Clinton currently leads the pack. True, she has never run anything herself, and her most notable foray into governance, her 1993-94 attempt to reform the American health-care system, was a catastrophe. But she has learned from watching the rest of her husband's presidency and, more recently, as a senator for New York, where she has been hard-working, consensual, effective and a little dull. Her campaign is superbly organised. In debates, her mastery of detail is remarkable. Her second plan for health-care reform is a much more moderate beast. And her Democratic rivals, Mr Obama and John Edwards, have much less experience than she does. On the Republican side, though, she faces a couple of effective governors and a former mayor of New York who turned that city's finances and crime rates around. She has yet to spell out much of her policy platform, including on such vital issues as tax or climate change; and has suspiciously meddlesome tendencies. She has already retreated alarmingly from her husband's commitment to free trade.

After competence must come toughness on security: traditionally a difficult area for Democrats, but less so after seven years of incompetent machismo. More than any of her Democratic rivals, Mrs Clinton has striven to neutralise the Republicans' advantage here. She has refused to apologise for her 2002 vote in favour of war with Iraq, and declines to commit herself to withdrawing the troops that are still there. But she was fully involved earlier this year in Democratic attempts to saddle the president with a deadline for quitting, and remains vulnerable to a Republican challenger. America's military weakness during the Clinton years has been overshadowed by the disaster under Bush; but it was under Mr Clinton that al-Qaeda took root and grew. That said, Americans want a tough president, not a psychopath: some of her Republican rivals remain worryingly bellicose.

Hillary the healer?

The third challenge for the next American president requires a different set of qualities: he or she will have to be a healer, both at home and abroad. America's standing in the world has been hugely damaged by the war, by Guantánamo and Abu Ghraib, and by the high-handed way in which it has treated international bodies and agreements. The country needs a leader who will rebuild alliances. Hillary Clinton has no direct experience of this, but she has already declared that Bill would be her “ambassador to the world”. His charm may help make up for the superpower's tendency towards unilateralism; though foreign leaders may be as uncomfortable as some Americans with the idea of an unelected spouse swanning round the globe representing America.

At home, Mrs Clinton will need to narrow the divisions that the bitter partisanship of the Bush presidency has widened. She can be an unforgiving enemy—witness her campaign's hysterical reaction when a Hollywood mogul went over to Mr Obama's camp. In recent years she has not given much impression of feeling anyone's pain but her own, though she is a funnier and warmer speaker than she gets credit for. Can such a woman, whose “negatives” are among the highest in the business, reunite America? This doubt remains a big obstacle to a Clinton comeback.

For all her years of scheming and positioning, Mrs Clinton is not the finished article. No process is better at revealing flaws than American presidential elections. This newspaper, like many voters, will reserve judgment on this still often awkward and unknowable woman until it has seen more of her and her policies next year. But so far the Clinton comeback has been impressive. That is why it is her presidency to lose.

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Myanmar

Life beyond the pale

Oct 4th 2007
From The Economist print edition

The outside world seems powerless to help the benighted country

EPA

Get article background

“NORMALCY” has now returned to Myanmar, boasted its foreign minister, Nyan Win, to the United Nations General Assembly this week. Sadly, he was right. It is normal for the country to be in the grip of vicious repression, with 15,000 soldiers keeping order on the streets of the largest city, Yangon; normal for unknown numbers of peaceful protesters to have been killed and for others to vanish into the Burmese gulag; and normal for the country to retreat into its default mode, isolation, with internet connections and mobile-phone lines largely cut. Days of brave protests, led by monks, had given a glimpse of the hopes that people power has brought to many countries, from the Philippines to Ukraine. But people power meets its match in a regime ready to kill and torture as many as it takes to cling to power. Myanmar's junta fits that bill.

Sadly, too, it is also entirely normal that the outside world is at a loss about how to react. And rather than speak in one outraged voice, it is giving these thugs the comfort of mixed messages. The divisions run along predictable lines. On the one side is the West, wringing its hands and thundering impotently. America, which already has tough sanctions against Myanmar in place, was swift to announce even tougher ones. Some in Congress want secondary sanctions against China, calling for a boycott of next year's Beijing Olympics.

On the other side are the Asian countries that have “engaged” rather than shunned the junta. Most important are China, India and Myanmar's fellow members of the Association of South-East Asian Nations (ASEAN). They, on the whole, are wagging fingers sternly at the misbehaving generals, but not threatening any sanctions. They seem to be waiting for the storm to pass and business-as-usual to resume, as it has in part since 1988, the last time the junta spilled a lot of blood to stay in power. But ASEAN, above all, has a duty to act in the face of one of the biggest tests the group has faced.

In one sign of a fragile international unity, the United Nations special envoy, Ibrahim Gambari, visited Myanmar (see article). And the Human Rights Council, on which China has a seat, adopted a resolution that “strongly deplores” the repression (“condemns” was apparently too interventionist for the squeamish Chinese). Even that went further than India, whose foreign minister hoped that “the process of national reconciliation” in Myanmar “would be taken forward expeditiously” and tentatively suggested the junta hold an inquiry into “recent incidents”.

ASEAN's mid-life crisis

An ASEAN statement departed from the group's habitual timidity to express “revulsion” at the violence and call for the release of all political detainees, including Aung San Suu Kyi, the opposition leader. For the sake of its own credibility, ASEAN will have to do more. It admitted Myanmar as part of its 30th-birthday celebrations in 1997, brushing aside criticism with the promise that engagement would help civilise the generals. This always seemed a convenient fiction to help ASEAN's loggers to strip the teak forests, its jewellers to scoop up rubies and Thailand's electricity authority to buy Burmese gas.

If engagement was supposed to buy influence, now is the time to use it. As ASEAN celebrates its 40th birthday, one of the world's most loathed regimes should not be helping to blow out the candles. Its continued membership of the organisation should be made conditional on its embarking on a genuine transition to civilian rule. ASEAN has never known where to set the bar for acceptable behaviour among its members. But wherever it is, it is surely too high for Myanmar.

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Russia

Democracy, Soviet-style

Oct 4th 2007
From The Economist print edition

The Russian people are readier for democracy than Vladimir Putin will allow

AP

THE timing was surely no accident. On October 1st newspapers in Moscow were idly speculating over who might be Ukraine's prime minister after yet another indecisive election. This was the moment when the Russian president, Vladimir Putin, chose to announce that he would head the pro-Kremlin United Russia party's list in the general election in December, adding that it was “entirely realistic” that he might become prime minister when his presidency ends in March.

This tale of two prime ministers speaks volumes for the state of democracy in the two neighbours that sprang from the former Soviet Union in 1991. Mr Putin's slide into autocracy since he became Russia's president in December 1999 is well documented, as are his background in and his zealous promotion of the Russian secret service. In nearly eight years in the Kremlin he has crushed opposition, stripped regional governments of their autonomy, reasserted state control of Russia's energy resources and eliminated most independent media.

Yet thanks to the stability that he has brought, and even more to oil-and-gas-fired growth, Mr Putin remains extremely popular with ordinary Russians. Indeed, the only real question among Moscow's chattering classes this year has been how he will retain his grip on power after next March, since the constitution sets a limit of two consecutive terms for a president. Now that question has been answered (see article). Wary of a crude constitutional change, and keen to avoid unflattering comparisons to the presidents-for-life of central Asian ex-Soviet republics, Mr Putin will find a placeman to stand for president (perhaps the man he just plucked out of obscurity to be his own prime minister, Viktor Zubkov). He himself will then take the post of prime minister, which he held briefly in 1999, probably with enhanced powers. After a decent interval, he could then return to the Kremlin as president.

Nowhere in these manoeuvrings is there a trace of democracy as understood and practised in the West: it is far more reminiscent of the old Soviet Union. Mr Putin's supporters maintain that Russians are not ready for liberal democracy, preferring their tradition of a benevolent dictator/tsar. They contrast the stability and prosperity of the Putin years with the chaos and poverty of the Yeltsin years. Some go further, echoing Mr Putin's view that, even if nobody wants to return to communism, the collapse of the Soviet Union was still the greatest geopolitical catastrophe of the late 20th century.

The Ukrainian model

Many Russians also point gleefully to the chaotic politics of Ukraine as just what they want to avoid. In fact Ukraine offers them a proud example. It is true that the country's politics has been messy since the

“orange revolution” of late 2004 propelled Viktor Yushchenko into the presidency, ahead of Russia's preferred candidate, Viktor Yanukovich; that Ukraine's wealthy business clans have too much political influence; and that corruption is entrenched (as it is in Russia).

Yet the election on September 30th was still a thoroughly democratic and unpredictable affair, more honestly conducted than any before it. After some hard bargaining, it seems likely to produce a new orange coalition government (see article). There is no longer serious talk of the country breaking apart: all political parties want to move closer to Europe. Unlike Russia, Ukraine now has independent media, a real opposition and the prospect of a genuine presidential contest in 2009. It also has a fast-growing economy that is likely to get into the World Trade Organisation before Russia does.

What can the West do to promote the democratic cause in the post-Soviet space? The answer in Russia is: not much. Mr Putin is sensitive to outside criticism, but not enough to make him more democratic. Western economic leverage over Russia is limited. Indeed, the bigger risk is that the Russians' stranglehold on gas supplies to Europe is putting more leverage into their hands. Tellingly, the Russian energy giant, Gazprom, this week again threatened to cut supplies to Ukraine.

But the West could do more to foster and encourage fledgling democracies in places such as Ukraine and Georgia, through better trade access, more favourable visa arrangements and stronger support in the face of Russian bullying. The European Union would also do these countries a huge favour if it were willing to hold out the prospect, however distant, of their becoming members. This has worked wonders in central and eastern Europe, and in the Baltics—there is no reason why it should not do so in other bits of the former Soviet Union. Above all, the successful establishment of working democracy in countries like Ukraine offers the best hope of one day luring Russia down the same road.

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Indian business

Untouchable and unthinkable

Oct 4th 2007
From The Economist print edition

Hiring quotas would not help lower-caste Indians and would harm business

AFP

Get article background

BUSINESSES in India are used to bad government. Indeed, this hardship has proved perversely useful: through coping with rotten infrastructure, throttling labour laws and mutable investment policies, many world-class Indian companies have emerged. A proposal to force firms to hire more workers from the dregs of Hinduism's caste system (see article) would be different. It would be a disaster.

India's long history of affirmative action springs from decent instincts. The caste system is possibly the world's ugliest social system. And it is sanctified by India's largest religion: according to the Laws of Manu, an ancient Hindu text, anybody from the lower orders who has the temerity to mention the name of a higher caste should have a red-hot nail thrust into his mouth; if he makes the mistake of telling a brahmin what to do, he gets hot oil poured into his ears and mouth.

Fortunately, India has moved on a bit since then. But socially and economically the place is still sharply stratified. Upper castes get a far larger share of good jobs than do lower castes; *dalits*—or untouchables—get virtually none. Which is why, soon after independence, India's government used affirmative action to try to redress the balance; and why calls for that action to be extended to business are so loud.

Affirmative action necessarily has a cost, both in fairness to those who in its absence would qualify for jobs and educational opportunities that they are denied, and consequently in efficiency. Still, if it went a long way to righting a big historical wrong, that might be justifiable.

But that hasn't happened in India. Nearly a quarter of university places and public-sector jobs have been reserved for *dalits* and tribal people since 1950; and, in 1993, a successor government handed a further quarter over to “other backward classes”. Yet there is no evidence that this has made any difference to the fortunes of the lower orders. They have certainly been getting richer—but, over the past two decades, at almost exactly the same rate as the rest of the population.

What's more, the policy has had dangerous side-effects. Cynical politicians promise their fellow caste members more jobs and university places. Reservation inflation has therefore been on the rise, infuriating the losers. As a result, battles over reservations have become a common source of riots, and politics has thus become increasingly polarised along caste lines.

Extending into the private sector a policy that has been a disaster in the public sector is lunacy. This

must be clear to India's prime minister, Manmohan Singh. As finance minister in the early 1990s, he started dismantling a system of industrial quotas, thus unleashing the economy. He should understand better than anyone the likely effect of introducing a quota on people. Yet he has been threatening to impose penalties on companies that don't hire more low caste workers.

Don't blame business

Reservations in companies would not just damage business. They would also distract attention from the real source of the problem. Responsibility for lower castes' lack of advancement does not lie with the private sector. There is no evidence that companies discriminate against them. The real culprit is government, and the rotten educational system it has created.

Originally, reservations were supposed to be needed only for a decade. After that, it was reckoned, they would be unnecessary, because primary education would be universally available. Nearly six decades on, it is not. And the quality of much of India's higher education is execrable. By one reckoning, only a quarter of engineering graduates, the raw material of a booming computer-services industry, are employable. The government should concentrate on sorting out schools and universities, not piling new burdens on business.

There's another effective weapon against ancient prejudices: growth. As Indians get richer, their caste biases fade. Middle-class urban Indians are less likely to marry within their caste than the rural poor, and less likely to wrinkle their noses at a *dalit*. Happily, the ranks of the middle class are swelling in a fast-expanding economy—for which India has its businessmen to thank. Hobbling them with quotas will only make it harder for them to help the country change.

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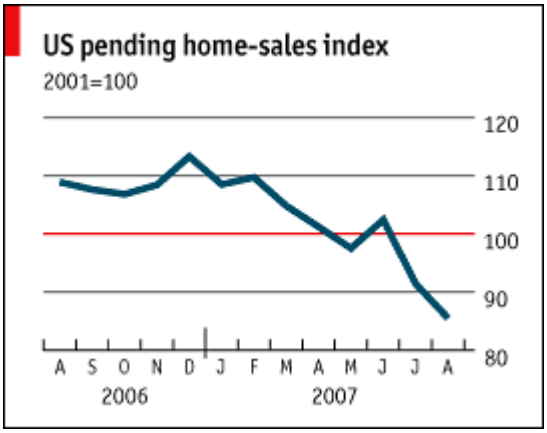
America's housing giants

Don't free Fannie and Freddie

Oct 4th 2007
From The Economist print edition

Letting them grow is no solution and could even be dangerous



THE news from America's housing market is getting no better. This week's helping of woe was a further sharp drop in pending home sales, an indicator of where the market is heading next. As sales plummet and defaults and foreclosures climb, pessimists fear that over a million Americans could be turfed out of their homes as adjustable-rate mortgages are reset (see article). What should policymakers do? An expansion of the Federal Housing Administration, which guarantees mortgages to iffy borrowers, is on the cards. But Congress is itching to do more: hence the calls to expand the role of Fannie Mae and Freddie Mac, the giant government-sponsored enterprises (GSEs) that tower over America's mortgage market.

Fannie's and Freddie's political allies want two things. The first is the raising of the $417,000 limit on the size of loans that the pair may handle. This would allow the GSEs into the “jumbo” mortgage market, where interest rates jumped in August. The second demand is the lifting of caps on the amount of mortgages they may buy and hold for themselves, put in place after accounting scandals a few years ago. Fannie and Freddie could then, as they portray it, ride to the rescue of struggling borrowers, injecting liquidity into parts of the market that have seized up. Their arguments are winning support, and opposition from the Bush administration and the GSEs' regulator—which has already raised the caps a little—is softening. Unfortunately, the ideas are likely to do more for Fannie and Freddie than for the mortgage market.

Start with the $417,000 limit. Lifting this—Freddie Mac suggests $650,000—could help if Fannie and Freddie scoured the upper bracket for borrowers who were struggling but viable. But their history suggests that they would cherry-pick those who could get refinanced elsewhere. And the jumbo-mortgage market may be correcting itself anyway: spreads over GSE-backed loans, though still unusually high, are falling.

There are two reasons not to let the GSEs' portfolios expand. First, it would be redundant. Whatever good Fannie and Freddie can do with bigger portfolios, they can already do through their other main business, guaranteeing and securitising others' mortgages, on which there are no limits. Fannie and Freddie would prefer to hold mortgages rather than guaranteeing them for a simple reason: it is more profitable.

It is also riskier. When they hold a mortgage, they take on not only credit risk but also interest-rate and prepayment risk. The loans they guarantee, in contrast, carry only credit risk (the other risks are borne by the investor in the securities). So as well as being just as effective, the guarantee business is also safer—and thus better for the taxpayer who unwittingly stands behind the GSEs. It is worth recalling that when Fannie and Freddie were caught mis-stating earnings by a combined $11 billion a little while ago, the mismanagement of interest-rate risk, not credit risk, caused their problems.

The dangers of privilege

Moreover, even if they grow no more, the mortgage giants pose a clear systemic threat. Their portfolios of retained mortgages and mortgage-backed securities add up to no less than $1.4 trillion. It is bad enough that this is concentrated in two institutions. Worse, they lack discipline because of the implicit guarantee. No matter how much risk they take or how they manage it, they can borrow at rock-bottom interest rates. If they got into trouble, banks as well as taxpayers would be on the hook. Banks may hold

as much GSE debt as they want. Many have amounts that exceed their regulatory capital.

It would be better if instead of letting Fannie and Freddie become even more bloated, politicians saw the GSEs for the anachronism they are. They were set up decades ago to help banks pool concentrated regional mortgage risk and to make housing more affordable. But as the market has grown deeper and more sophisticated, history has left them behind—hence their desire to get into any bit of the business that will turn a profit. The eventual aim should be to turn them into normal private-sector companies, by stripping them of the charters that give rise to the implicit government guarantees, and break them into smaller pieces. Encouraging another growth spurt, even in today's sagging market, is asking for trouble.

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On civil liberties and freedom, nuclear power, lighting, computers of the future, Standard & Poor's, Burlington House

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From The Economist print edition

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Free to disagree

SIR – You argue that eschewing civil liberties in the name of greater security will only result in a "slippery slope" where an omnipotent state has a complete disregard for the basic rule of law ("The real price of freedom", September 22nd). Yet in an age when the enemy is as atomised as al-Qaeda or the Taliban, one could argue that the reverse is actually true. That is, when the state is paralysed by an unfettered deference for individual liberties, a slippery slope of an entirely different kind emerges and our enemies ably exploit our wobbly defences to inflict far greater pain and suffering than the suppression of certain freedoms could ever be capable of.

That America has yet to experience an act of terrorism as menacing as what happened six years ago is truly beside the point. What does matter is how we approach this mildly utilitarian discussion. Your article attempts to settle the debate; the truth, however, is never as simple as a slippery slope tilting in one direction.

Samuel Pavel
Brooklyn

SIR – Your argument that dropping practices which violate human rights would be worth the cost in lives if freedom was protected makes little sense. The last time I checked, the right to life was itself a fundamental human right. Furthermore it is the only one for which you cannot be justly compensated if it is denied to you. I am confident that most people, given the choice between suffering even such horrors as torture and imprisonment, or losing their own or the lives of loved ones, would willingly undergo the former. Of course there is a "slippery slope" and we should not be glib about sacrificing vital freedoms. But nor should we be glib about the cost of "many lives" if we do not make some compromises with that freedom.

Robin Conway
Oxford

Nukes new and old

SIR – You ignore important subsidies to the American nuclear industry, but repeat its most pernicious myths ("Atomic renaissance", September 8th). The Price-Anderson Act and its 2005 expansion shift the insurance burden for nuclear accidents from utilities to taxpayers. Nor does the $.001/kilowatt-hour Nuclear Waste Fund fee cover the anticipated costs of radioactive waste. If industry bore these costs, there would be no nuclear resurrection.

Meanwhile, the Congressional Budget Office predicts a 50% or higher default rate on taxpayer-backed loans to nuclear utilities enabled through the 2005 energy bill, now being considered in Congress for a tenfold expansion. You are right: nuclear power is now "too expensive to matter."

Michael Mariotte
Executive director
Nuclear Information and Resource Service
Washington, DC

SIR – You describe the causes of the Chernobyl disaster to be "a combination of operator errors and

inherent flaws in the plant's design" ("Nuclear dawn", September 8th). The real cause was not operator- or even industry-related. Soviet scientists were authorised to carry out experiments that required the reactor to be pushed to or beyond its limits, with safety features disabled. Consequently, meltdown occurred. This is documented by both Western and Soviet sources. All reactors have elaborate safety features to guard against similar disasters; proof lies in there having been no other Chernobyls. It is hard to imagine any nuclear power plant owner allowing the same misuse to occur again.

Philip De Groot
Toronto

SIR – Your assertion that fears of nuclear power may be overblown, citing a figure of around 4,000 eventual deaths from the Chernobyl accident, is extraordinarily short-sighted and misleading ("Nuclear power's new age", September 8th). Are the continuing birth defects and the death of the surrounding region irrelevant?

Michael Grove
Boston

Bright green

SIR – The "huge amounts of electricity" that are required to power incandescent lamps are not wasted, as you believe ("Everlasting light", September 8th). The heat generated by incandescent bulbs contributes to the overall heating level. If households replace incandescent lamps with fluorescent ones, people will compensate for heat loss by switching on or cranking up central heating.

We must also recognise that the environmental costs of fluorescent bulbs are comparatively very high. They contain plastics, mercury, phosphors, tin, lead, copper, silicon and circuit boards, all of which are extremely difficult to recycle when combined in a lamp with its built-in disposable control gear. It is no secret that the cost of packaging, importing and disposing of these "environmentally friendly" lamps is enormous when compared with the humble traditional light bulb. The new lamp from Ceravision that you mentioned won't need to be replaced very often and should help with this problem.

Theo Paradise-Hirst
Head of lighting design
Max Fordham Consulting Engineers
London

Movie file

SIR – It is ironic that you chose Steven Spielberg's film "Minority Report", set in 2054, to illustrate a dramatic vision of what the future might hold for computer user-friendliness ("The trouble with computers", September 8th). The film has a scene in which a file is stored on a sort of floppy disk, carried across a room, and opened on another computer. I sincerely hope that computer-network technology has not regressed to the point of non-existence by the mid-21st century.

Caspar von Wrede
Berlin

Credit where it's due

SIR – The timing of my departure from Standard & Poor's may have confounded some analysts of the news. But contrary to your suggestion there was no knife to fall on, kitchen or otherwise ("Credit and blame", September 8th). The decision to step down was carefully considered, long-planned and of my own initiation.

It is not an easy decision to change one's career after 25 years in the financial markets (the last 13 as a working mother), nor can such a decision be perfectly timed to fit credit market cycles. Nevertheless, my family is pleased, and I am pleased to have had the privilege of serving S&P.

Kathleen A. Corbet
New Canaan, Connecticut

Learned lessons

SIR – Burlington House, the home of the Royal Academy of Arts, was not built by “the government of a previous queen” in 1857 but by Lord Burlington with Colen Campbell and William Kent in 1715-21 (“Uproar at the aviary”, September 15th). The Learned Societies reside in 19th-century wings of Britain's first neo-Palladian building. When sold by the Cavendish family to the government in 1854, it had fallen from fashion: Lady Cavendish complained that its fine classical rooms were too narrow for hooped-skirted ladies to waltz in.

Sarah Greenberg
Royal Academy of Arts
London

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Hillary Clinton

Ready to run the movie again?

Oct 4th 2007 | WASHINGTON, DC
From The Economist print edition

The betting is that the Clintons will follow the Bushes back into the White House

AFP

THE September 29th issue of the *National Journal*, an inside-the-Beltway magazine, contains a striking news item. Hillary Clinton has quietly signed a deal with the University of Illinois to house her presidential library. The university will put up $15m to help finance the construction and operation of the huge building on its Urbana-Champaign campus, close to where Hillary Rodham was born.

This was, of course, a joke—but it contains a serious point. The political establishment is betting heavily that Hillary Clinton will become America's next president. And it has reason. Mrs Clinton is way out in front of the Democratic field. The latest *Washington Post*/ABC News poll puts her 33 points ahead of Barack Obama and 40 points ahead of John Edwards. She raised $22m in the last quarter—more than Mr Obama at $19m and much more than Mr Edwards at $7m. The once-mighty Republican Party is a shadow of its former self, divided not only about who should lead it but also about where it should go. Intrade, a pay-to-play prediction market, shows a 36% chance of the Republicans holding the White House alongside a 12% chance of them taking the House and a 7% chance they might take the Senate.

Politicos invariably hedge all this around with qualifications. Howard Dean was well ahead of the Democratic field at this stage of the electoral cycle in 2004. Mr Obama might make a breakthrough in Iowa (where he is nipping Mrs Clinton's heels) and gain enough momentum to win the nomination. Mrs Clinton might stumble and fall. The American electorate might balk at the idea of handing both the White House and Capitol Hill to a single party and go for a Republican president. All possible, of course; but all less likely by the day. Mrs Clinton is not only the front-runner. She is well on the way to becoming a prohibitive front-runner.

This is an extraordinary situation, for all sorts of reasons. The race ought to be wide open: it is the first time that neither party has an incumbent, in the form of a vice-president, since 1928. The rise of the netroots has transferred political power from the Washington establishment to smaller donors. And America is in an anti-establishment mood: the Democratic Congress has even lower approval ratings, at about 27%, than George Bush. Yet Mrs Clinton has all the advantages of an incumbent, from a brand name to an established political machine, without many of the disadvantages.

And this too is odd, since she is one of the most hated figures in American politics. During the 1990s she embodied everything that conservatives hate about female professionals: a bossy harridan who disparaged stay-at-home mothers, tried to reorganise the health-care system that makes up one-seventh of the American economy, and stayed with her tom-catting husband to further her political ambitions. Conservative conferences regularly feature loo-paper with Hillary's face on it and Hillary trolls to throw balls at. CafePress, a web retailer, is selling more than 100,000 anti-Hillary items, including a “Hillary is the Devil” beer stein.

But Hillary-hatred is by no means confined to the right. David Geffen, a Hollywood mogul, gave voice to a

widespread feeling on the left when he complained about the Clintons' relationship with truth. “Everybody in politics lies,” he told the *New York Times*. “But they do it with such ease, it's troubling.” Mrs Clinton has some of the highest negatives of any politician in the business.

And yet here she is, with her husband, looking likely to break all sorts of records. If she wins, Mrs Clinton will be the first female president of the United States—a banner headline in itself—and Mr Clinton will be the first male first spouse. She will be the first president married to a former president. She will also be the first president who is married to a former president who was impeached for having oral sex with an intern in the Oval Office.

This raises all sorts of intriguing questions. How will the first couple be addressed? Mrs and Mr President? Mrs President and Mr Clinton? What will people call Mr Clinton? (He says that his Scottish friends have suggested “first laddie”.) And, more important, what will Mrs Clinton do with her husband? Back in 1992, the Clintons campaigned on the slogan “Buy one, get one free”. But Mrs Clinton's presidency will be doomed if she allows herself to be overshadowed by her more experienced and more charismatic spouse. Not for the first time, Mr Clinton is likely to be both her biggest asset and her biggest liability.

Senate training

The path for the Clinton restoration has been prepared by two things—an implosion and a fizzle. The implosion was provided by the Republican Party, thanks to a combination of runaway spending and incompetence. Five years ago America was evenly divided by party identification: 43% for each party. This year the Democrats have a 50% to 35% advantage. Democratic presidential candidates have raised about 70% more than their Republican rivals. Ohio, Virginia and Colorado are leaning Democratic, and Pennsylvania has gone from a swing-state to a Democratic lock.

The fizzle has been provided by Mr Obama. He is an impressive candidate who still draws bigger and keener crowds than Mrs Clinton, but his performance in the presidential debates has often been listless. His message of “new politics” and reconciliation can seem tired. He has failed to appeal to blue-collar voters who think that politics is about problem-solving rather than inspiration. The fact that he has now fallen behind Mrs Clinton in fund-raising, where he was once comfortably ahead, is dismal news for his campaign.

Mrs Clinton has also positioned herself brilliantly for a presidential run after the traumas of her White House years. She has moved to the centre at a time when powerful forces have been pulling her party to the left. She has softened some of her rough edges, if only cosmetically. And she has accumulated yet more political capital.

Her repositioning started with her Senate run in 2000. She chose to live in suburban Chappaqua, rather than Manhattan, in order to blunt her image as a liberal elitist. She focused on small-bore issues rather than grand schemes, and campaigned relentlessly in the more conservative farming districts. The result was that she won re-election with majorities not just in Manhattan but also upstate.

She also proved to be an exemplary senator. Trent Lott once mused that lightning might strike her before she set foot in the chamber; five years later, according to Joshua Green in the *Atlantic Monthly*, he became one of 49 Republicans who have sponsored legislation with her. She has been a regular at Senate prayer breakfasts, where something of the old bipartisan Senate survives. She has listened patiently to ancient denizens such as Robert Byrd (who advised her to be a “work horse not a show horse”). She could hardly have done better at managing her twin positions as junior senator and global celebrity.

Outside the Senate, Hillary has displayed the same singleness of purpose. She has relentlessly courted religious voters (whose relationship with the Republican Party is increasingly strained), describing abortion as a “tragic choice”, defining herself as a “praying person”, and employing evangelical Christians on her staff. She has repeatedly rebuffed attempts by the left to harden her opposition to the Iraq war, insisting that she will not foreclose any military options as president. She even appeared in a documentary about Barry Goldwater, praising the Arizona Republican and reminiscing about her first days in politics as a “Goldwater girl”.

She has also devoted a lot of effort to improving her party's infrastructure. She helped John Podesta, her husband's former chief of staff, to found a think-tank, the Centre for American Progress, which is a ready source of ideas and talent. She also supported the American Democracy Institute, which is run by

veteran Clinton allies, and Media Matters for America, a media watchdog group, which was founded by David Brock, a former Clinton-hater turned Clintonite. All this helped to ensure that, for all the energy unleashed by the netroots and Al Gore, the Washington Democratic establishment has remained a wholly owned subsidiary of the Clinton family.

Mrs Clinton's careful repositioning has gone hand-in-hand with her husband's rehabilitation. What might be called Mr Clinton's lapses of judgment have faded from the public mind. He likes to remind people that "yesterday's news was pretty good". His superstar status abroad is a rising asset in a country that is rightly worried about its global image. And Mr Clinton has had an energetic post-presidential career, raising piles of money for his charitable foundation as well as making a fortune for himself and forming a successful double act with George Bush senior, particularly after the tsunami in South-East Asia. He is now more popular among Democrats than when he left the White House, and more popular by far than his wife or any of her rivals. Some 88% of Democrats view him favourably.

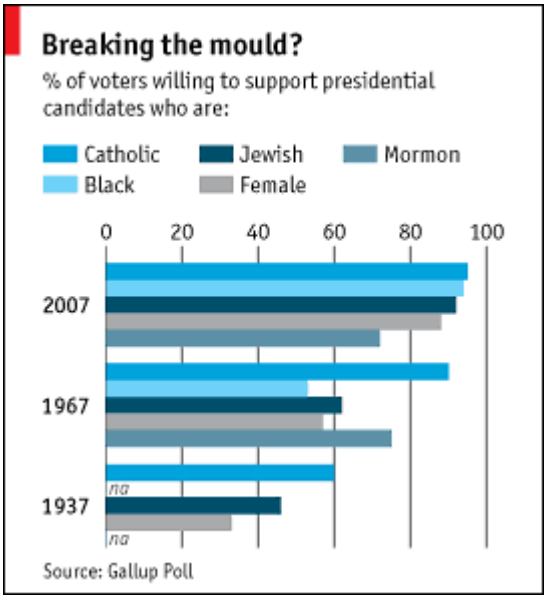
The final piece of the Clinton puzzle is her formidable campaign machine. Mrs Clinton has assembled the best collection of pollsters, image-crafters, fund-raisers and hatchet-men in the business; and so far she has managed them successfully. Her campaign has been relentlessly smooth, if a bit mechanical (she is forever bursting out laughing, whether it is appropriate or not, to counteract the idea that she has no sense of humour).

This is also a campaign with teeth. Tom Vilsack, a former governor of Iowa and close ally, told a cable news channel that the whole country would soon know as much about Rudy Giuliani's private life as New York knows already. Mr Clinton has also gone on record questioning whether Mr Obama has enough experience for the presidency, particularly in an age of terrorism. Mr Clinton had about as much experience in 1988, when he considered running but thought better of it.

Countering the negatives

Mrs Clinton still has strikingly high negatives: the latest Pew poll shows that 39% have an unfavourable view of her candidacy. But Mr Bush has proved that you can still win a presidential election while lots of people hate you. And Mrs Clinton is doing a goodish job of dealing with those "negatives"—certainly good enough to pick up many disillusioned Republicans and restive independents.

Her biggest potential negative is her sex. Americans are highly sensitive to the fact that the president is also the commander-in-chief—and Mrs Clinton is a graduate of a White House that had notoriously bad relations with the military world. Men are also much less well-disposed to Mrs Clinton than women: 45% of men have a negative opinion of her and only 36% have a positive opinion. The figures for women are 31% negative to 45% positive. If George Bush senior reminded women of their first husband, Mrs Clinton reminds men of their first wife.



Yet Candidate Clinton is not running as a feminist. She made a point of serving on the Armed Services Committee in the Senate. She is by far the most hawkish of the current Democratic candidates. She repeatedly emphasises that she is not running as a female candidate. Most Americans are happy with the idea of a female president (if not with this particular female). And the presidential field is full of people who are "different" in some way, from John McCain, the oldest man to run for president, to Rudy Giuliani, the most divorced man to run for president, to Mitt Romney, who is a Mormon, to Dennis Kucinich, who is, well, Dennis Kucinich.

Mrs Clinton's second-biggest negative is that very executive ability. Her biggest experience of running something, rather than bending her husband's ear or voting in the Senate, proved a disaster. What she advertised as the most ambitious domestic reform since FDR—her health-care plan—collapsed in ruins in 1994.

But again she has moved smartly to deal with the problem. Her latest health-care plan is much more modest than her last, and it puts a heavy emphasis on choice rather than bureaucratic reorganisation.

Given the level of worry in America about health care, among businesses as well as consumers, the Republicans will have to do more to discredit it than just resurrect taunts about “Nanny Hillary”.

Mrs Clinton now exudes an overwhelming air of competence. Mr Bush is widely regarded as one of the most incompetent presidents in American history—a man who rushed blind into Baghdad, who filled his administration with lacklustre cronies, who bungled the handling of Hurricane Katrina and who famously claimed that he could not think of a single mistake he had made. Mrs Clinton is the anti-Bush: a woman who speaks in clear sentences, who has a formidable command of the facts, and who, on health care, is willing to learn from her mistakes.

The trouble with dynasties

What does the possibility of a Clinton restoration mean for America? Everything depends on whether Mrs Clinton can translate her air of competence into reality. The Clinton White House, be it remembered, lurched from crisis to crisis, some of them of Mrs Clinton's creation. It is also worth remembering that Mr Bush sold himself as an MBA president surrounded by political veterans. But three things are already clear—one positive and two negative.

The positive is that Mrs Clinton would break America's highest glass ceiling. Women have made their mark in almost every area of American life, from the Senate (16 currently) to the House (74, including the speaker) to the governor's office (nine). Madeleine Albright and Condoleezza Rice have both been secretary of state. In that respect, a woman president would undoubtedly be a good thing for the country.

But there is a downside: dynasty. If Mrs Clinton wins the White House in 2008, members of the Bush and Clinton families will have been president for 24 years on the trot. Over 100m Americans have never known anybody but a Bush or a Clinton in the White House. If Mrs Clinton wins re-election, that 24 years will swell to 28.

Americans are remarkably insouciant about this development. They should not be. It suggests that American political life is in the hands of a small group of insiders who are organised around semi-royal families. And it divides America into “players”, who control political life, and “observers”, who simply comment on it. The dynastification of American politics is happening at a time when economic inequalities are growing, and the “haves” are proving increasingly successful at transmitting their privileges to their children.

The other negative side is that it freezes American political life. One of the virtues of the American political system is that it is supposed to produce shake-ups whenever a new president takes over. Mrs Clinton will bring back the same cast of characters that everybody wearied of in the 1990s, from slick money-raisers like Terry McAuliffe to professional conservative-haters like Sidney Blumenthal.

Back in 1993 Jacob Weisberg, writing in the *New Republic*, accused the Clinton team of “Clincest”—being a “tight, hermetic and incestuous clique” who went to the same universities and hung out at the same Democratic gabfests. Mrs Clinton's election will not only perpetuate “Clincest” for another four or eight years; it will also add another dollop of ageing baby-boomer self-satisfaction. During a campaign speech earlier this year Mr Clinton remarked that he once told Hillary, when they were both students at Yale, that “I have met all the most gifted people in our generation and you're the best.” This sort of attitude will be difficult to live with.

The Clintonites have already brought back some of their old bad habits. Mrs Clinton had to return $850,000 from a fund-raiser called Norman Hsu who turned out to be a fugitive. But even more dispiriting will be the continuing polarisation of American politics. Mrs Clinton may have damped down Hillary-hatred for a while. But it is sure to revive if she starts appointing Supreme Court justices. And Mrs Clinton is still surrounded by the same fanatically loyal and combative staff that she had in the 1990s. America will be stuck not just in the same tired culture war, but also in the same culture war fought by the same characters. The potential for further alienation from politics, particularly after the Bush years, will be huge.

Mrs Clinton is clearly a formidable candidate for the presidency. She has the most powerful name in the business now that the Bush brand is tarnished. She has a smoothly working political machine. She has a wealth of experience in both the legislative and the executive branch. And she exudes competence. All told, she looks likely to translate this into both the Democratic nomination and a victory in November

2008. But whether a Clinton restoration will be good for America is a much more difficult question.

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America's property crisis

The hammer drops

Oct 4th 2007 | MAPLE HEIGHTS AND SAN BERNARDINO
From The Economist print edition

Illustration by Satoshi Kambayashi

America's houses are being repossessed at a record rate. What comes next?

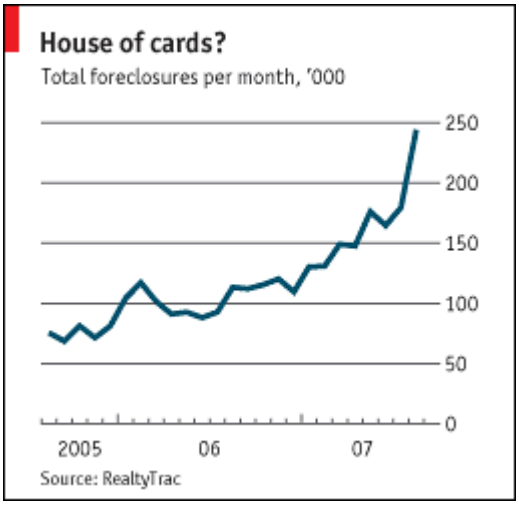
AT FIRST sight, Maple Heights, just outside Cleveland, looks much like any other ageing suburb in the industrial mid-west: a patchwork of small colonial-style houses built after the second world war, with leafy streets and mown lawns. Up close, it is a community in collapse.

Every twelfth house stands empty, repossessed after its owner defaulted on a mortgage. There are no boarded windows (a local ordinance forbids them) and the city council cuts the grass around vacant homes. But the cracked panes, crumbling paint and rotting porches are hard to hide. Countless more homes sport “For Sale” signs as the remaining owners try to flee to better areas. With so many houses vacant, the property tax base has crumbled. Since 2003, the local government has laid off 35% of its staff.

As America's housing bust grows ever deeper, the big question is how far Maple Heights is a harbinger of things to come. Nationally, people are defaulting on mortgages at a faster pace than at any point in recent decades. According to the Mortgage Bankers Association, some 5% of all mortgages are delinquent and the share rises to almost 15% for “subprime” mortgages—those lent to people with shaky credit histories. In the second quarter of 2007, almost 3% of subprime loans entered foreclosure (the process of default and repossession). RealtyTrac, a company that tracks foreclosures, reckons up to 1.5m households will enter the process this year (see chart), double last year's figure. And with some 2.5m adjustable-rate mortgages resetting to higher rates before the end of 2008, everyone knows there is much worse to come.

The pain will probably be concentrated in two main areas. One, typified by Maple Heights, is the Midwest—states such as Ohio and Michigan, where the subprime bust is battering an industrial economy already in long-term decline. The other is quite different: booming states, such as Florida and California, where the subprime bonanza fuelled the biggest housing bubbles. Until recently, the highest default rates were in the industrial heartland. But that is changing fast. More than a third of all adjustable subprime loans are in California, Nevada, Arizona and Florida. California alone has 17% of them, and the numbers are soaring. In Riverside and San Bernardino counties, two sprawling counties east of Los Angeles that comprise an area called the

“Inland Empire”, 1,900 houses were repossessed in August. It was 31 a year earlier.



The good news is that high default rates may be less painful in places whose sub-prime problem sits atop an economic boom. Cleveland has been losing inhabitants for years. In contrast, almost 800,000 people piled into the Inland Empire between 2000 and 2006, swelling the population by a quarter. The area is the main distribution hub for Chinese imports, and it has added 50,000 jobs in the past year.

The bad news, though, is that foreclosure is costly and high rates of it can cause plenty of collateral damage. In Cleveland, lenders incur legal fees and other costs of around $25,000, or 25% of the value of a typical subprime loan. The process of repossession takes a year or more, during which delinquent borrowers have little reason to look after their homes. A glut of repossessed houses dampens prices, and not just by adding to the supply of homes for sale. Thanks to high commodity prices, vacant homes in poorer neighbourhoods are quickly stripped of their aluminium sidings and copper fixtures. Marginal houses become uninhabitable; crime rises; whole areas are blighted.

Add these costs to the human toll of people being turfed out of their homes, and it is no surprise that America's politicians are scrambling for ways to stem the foreclosures. (All the more so because hardest-hit areas include election swing states such as Ohio and Florida.) So far, the focus is on low-cost intervention: encouraging borrowers to seek counselling and lenders to show forbearance. The Senate has appropriated $100m to help community groups advise delinquent borrowers. A national foreclosure hotline offering free advice gets 2,000 calls a day.

These efforts will help. A rough estimate is that half the people who are likely to face foreclosure in the coming months could service a renegotiated loan. But Cleveland's experience suggests the process is not easy. According to Lou Tisler, head of Neighbourhood Housing Services of Greater Cleveland, a local community group, mortgage lenders are becoming more willing to renegotiate loans. But most people seek advice only after they have been in default for months. Many are only days away from the sheriff's sale at which their home is formally lost.

Cleveland's experience also shows the limits of the small-scale public bail-outs to help “victims”. Politicians have a weakness for such schemes. Ohio's state government was the first to set up an explicit foreclosure rescue fund: it has promised $4.6m to help distressed homeowners who earn up to 125% of their county's median income. The state will put up to $3,000 towards mortgage refinancing. Some 250 people have been helped thus far; the goal is 1,500. But with 150,000 Ohio mortgages resetting over the next 12 months, the bail-out is a drop in the bucket. The only type of rescue that would prevent a surge in foreclosures would be a huge federal bailout which no politicians (as yet) are contemplating.

And the hard truth is that in many cases preventing foreclosure is a bad idea. Not all defaulting borrowers are suffering families. In the bubbliest property markets, many mortgages are held by investors, who were speculating on higher prices. In Florida, a quarter of all defaulting loans are held by non-residents. Even in Cleveland, many subprime borrowers are in houses that they cannot—and will not be able to—afford. Foreclosure is, unfortunately, the right outcome for perhaps half of America's problem mortgages.

That suggests politicians should put more emphasis on making the process more efficient. Already there are vast differences between states. In New York it takes at least 15 months for a house to be repossessed, according to Rick Sharga of RealtyTrac; in California it takes at least four months, while in Texas delinquent homeowners can lose their house less than a month after receiving a formal notice of default. That is extreme, but relatively speedy repossessions might at least reduce some of the collateral damage.

All told, the biggest unknown about America's subprime bust is how quickly, and how far, house prices will have to sink. Nationally, house prices have fallen by some 3%, while the glut of unsold homes has risen to ten months' supply. In the areas hardest-hit by defaults, the glut is far bigger. But rather than prices adjusting further, sales have simply dried up. In the Inland Empire the number of houses sold has halved in the past year. Michael Ciaravino, the mayor of Maple Heights, points out that only three houses have sold in the past two months, compared to a monthly total of between 15 and 50 a few years ago.

Once prices halve, he reckons, the market will clear, new families will come in and his suburb will recover. The question, for Maple Heights and America, is how much damage is done in the meantime.

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Health insurance

Happy-go-lucky young

Oct 4th 2007 | AUSTIN
From The Economist print edition

The latest targets for insurers

YOUNG people are hard to pin down. They graduate from school. They jump between employers, or in and out of employment. They leave their parental home for a shared flat, a friend's couch, or a house they can scarcely afford. They move to New York, San Francisco, Portland, or even Austin.

And so they often wander away from the comforts of health-care insurance. According to the Census Bureau, almost 30% of Americans between the ages of 18 and 34 are uninsured. For people aged 45 to 64 the number is just 14%.

A healthy young person seldom requires medical attention. So forgoing insurance is an understandable decision. But some of those who roll the dice lose. A serious illness or accident can be financially ruinous, and lead to sub-standard care.

Having more healthy young people in the insurance pool would benefit insurers, because they are less likely to make big claims. But efforts to attract them have thus far been feeble. Various companies offer low monthly premiums aimed at the young. But they typically have high deductibles—the amount the subscriber has to pay out of his own pocket before insurance kicks in. So young people tend to shy away from them.

One company, however, is taking an interesting new approach. In September Precedent Insurance—a division of the American Community Mutual Insurance Company—brought out a line of Coverage on Demand plans. The plans are currently available only in Texas, which has a higher percentage of uninsured people than any other state. They offer low premiums, low deductibles, limited benefits, and a clever twist. If you exhaust your benefits but need more coverage, you can pay an additional “activation fee” and get more, even after you get ill or hurt. There are four levels of cover. To get to the fourth requires at least a cumulative $9,000 in activation fees. But it then provides the subscriber with up to $5m in coverage.

The activation fees for the higher levels are steep, but a lot better than bankruptcy. According to Mike Grandstaff, the company's chief executive officer, they only make sense if you are, in fact, in reasonably good health. If you are likely to need more than the first level of coverage, the plan is not really economical.

Even people who plan on staying well may prefer more comprehensive health-care insurance. The Precedent plans do not cover, for example, costs associated with a normal pregnancy. This is to discourage women who plan on becoming pregnant shortly after signing up. But it is, of course, hard luck on a woman with an unplanned pregnancy. Perhaps she could hope that the father works for the government and is in a marrying mood.

Young people have it tough. It remains easier for politicians to rally around the cuddly or wrinkly. This was apparent this week, as Democrats denounced a “cruel” George Bush for vetoing, on October 3rd, the reauthorisation and expansion of the State Children's Health Insurance Programme (SCHIP). This federal programme provides insurance for 6.9m children from low-income families by providing blocks of money to the states, which disburse it. SCHIP began in 1997 and expired on September 30th, although Congress has already extended it for six weeks while the political wrangling continues.

A bipartisan majority in the House and Senate passed a plan that calls for $35 billion in additional spending on SCHIP over the next five years, only to see it vetoed as expected. The plan would have upped the number of children covered to 10m. Mr Bush opposed the scheme mainly on cost grounds (though Democrats say this rings false, given how much he is wasting on the Iraq war) and accused him of wantonly denying children health-care insurance. This week they plainly won the political advantage.

But curing America's health-care system will take more than political point-scoring and limited fixes. It will require a degree of political co-operation that is not now available.

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Urban politics

Not in my front yard

Oct 4th 2007 | CHICAGO
From The Economist print edition

In a fight over Grant Park, Chicago's mayor faces a small revolt

RICHARD DALEY is used to getting what he wants. Elected Chicago's mayor in 1989, he is often called “the emperor”. Now he is facing a rare opponent: a 35-year-old, first-term alderman. Last month Brendan Reilly said he would fight plans to move the Chicago Children's Museum to a treasured spot in his ward, Grant Park, the city's so-called front yard. Mr Daley erupted, hinting that the museum's critics simply want to keep black and Hispanic children out of the park. He declared it “a fight for the future of this city”.

Mr Daley already seems sheepish about framing the fight in such dramatic terms. He has softened his tone and says he is open to compromise. But Chicagoans are still waiting for the details. For though Mr Daley can usually rally the city council to his side, Mr Reilly has claimed a powerful ally: Aaron Montgomery Ward.

True, Ward died in 1913, but he rules over Grant Park from the grave. Having made a fortune from America's first mail-order business, Ward went to court to keep developers out of the park. He based his case on the words of three commissioners, who in 1836 wrote that what is now Grant Park should be “Public Ground—A Common to Remain Forever Open, Clear and Free of any Buildings, or other Obstruction Whatever.” During his life Ward was often perceived as a stubborn pest—the *Chicago Tribune* called him a “human icicle”. But for decades he has been praised as the guardian of the park, which covers 320 acres (1.3 square km) along Chicago's lakefront.

Mr Daley has shown himself more flexible than Ward purists. One of his greatest achievements, Millennium Park, defies Ward's principle of pure open space. The park is dotted with attractions, including Frank Gehry's Pritzker Pavilion, which called itself a piece of art to dodge conflict over new construction. The park has been enormously popular since opening in 2004; last year it had 3m visitors.

Officials at the Children's Museum hope that a new home in Grant Park, just over a bridge from Millennium Park, would build on this success. But Tom Wolf of Friends of Downtown, a civic group, worries that the museum would be a precedent that would let other developers invade Grant Park.

The city council must approve the museum's move. Mr Reilly is telling his fellow aldermen to scuttle the plan. Abandoning him could set a bad example: if the aldermen do not stand together to fight this project, what power will they have to oppose future ones? And perhaps the aldermen are more wary of defying Ward's vision than the mayor's. All this makes for a rather unusual situation. Mr Daley may be the emperor, but in a fight over the city's most beloved park, cutting a deal may be the true mark of leadership.

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Washington

Capital of culture

Oct 4th 2007 | WASHINGTON, DC
From The Economist print edition

An intellectual and artistic renaissance

WASHINGTON, DC has traditionally been an unbalanced city when it comes to the life of the mind. It has great national monuments, from the Smithsonian museums to the Library of Congress. But day-to-day cultural life can be thin. It attracts some of the country's best brains. But far too much of the city's intellectual life is devoted to the minutiae of the political process. Dinner table conversation can all too easily turn to budget reconciliation or social security.

This is changing. On October 1st the Shakespeare Theatre Company opened a 775-seat new theatre in the heart of downtown. Sidney Harman Hall not only provides a new stage for a theatre company that has hitherto had to make do with the 450-seat Lansburgh Theatre around the corner. It will also provide a platform for a large number of smaller arts companies such as the Washington Ballet, the Washington Bach Consort and the CityDance Ensemble.

The fact that so many of these outfits are queuing up to perform is testimony to Washington's cultural vitality. The recently-expanded Kennedy Centre is by some measures the busiest performing arts complex in America. But it still has a growing number of arts groups which are desperate for mid-sized space downtown. Michael Kahn, the theatre company's artistic director, jokes that, despite Washington's aversion to keeping secrets, it has made a pretty good job of keeping quiet about its artistic life. The Harman Centre should act as a whistle blower.

Washington still bows the knee to New York and Chicago when it comes to culture. But it has a good claim to be America's intellectual capital. It has the greatest collection of think-tanks on the planet, and it regularly sucks in a giant share of the country's best brains. Washington is second only to San Francisco for the proportion of residents 25 years and older with a bachelor's degree or higher.

Washington's intellectual life has been supercharged during the Bush years, despite the Decider's aversion to ideas. September 11th, 2001, put questions of global strategy at the centre of the national debate. Most of America's intellectual centres are firmly in the grip of the left-liberal establishment. For all their talk of “diversity” American universities are allergic to a diversity of ideas. Washington is one of the few cities where conservatives regularly do battle with liberals. It is also the centre of a fierce debate about the future direction of conservatism.

The danger for Washington is that this intellectual and cultural renaissance will leave the majority of the citizens untouched. The capital remains a city deeply divided between over-educated white itinerants and under-educated black locals. Still, the new Shakespeare theatre is part of job-generating downtown revival. Twenty years ago downtown was a desert of dilapidated buildings and bag people. Today it is bustling with life. If Washington is struggling to fix the world, at least it is making a reasonable job of fixing itself.

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Teaching poor children

A hard road to hoe

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From The Economist print edition

Does the Teach for America programme really improve schools?

AS THE 58,000 pupils of the District of Columbia Public Schools (DCPS) begin a new school year, their teachers are adjusting to a controversial new boss. Michelle Rhee, a rookie superintendent, is an unusual choice to run one of the worst school systems in America. She is the youngest chancellor ever of DC's public schools and the first non-black to run the system in four decades. But the most interesting aspect of Mayor Adrian Fenty's choice is that Ms Rhee is an alumna of an outfit called Teach for America.

Only about half of Americans growing up in poverty complete high school, and those who do reach only an eighth-grade standard. In an effort to solve that problem, Teach for America (TFA) recruits top college graduates—usually people without teaching qualifications or experience—and asks them to spend two years teaching some of the nation's poorest children. “We need fundamental systemic change and we believe our people can help be a force for that,” says Wendy Kopp, TFA's founder and CEO.

A lot of people agree. *Business Week* honoured TFA as one of the best places to launch a career. Fast Company included it in a list of “Entrepreneurs who are changing the world”. And the organisation is popular; it has grown from just a few hundred corps members in 1990 to more than 5,000 teachers in 26 regions today. It aims to nearly double in size by 2010, and has just announced plans to support similar programmes abroad.

The effectiveness of TFA teachers is hotly debated, however. Critics point to studies that say traditionally certified teachers perform better. Even some supporters worry that teachers don't stay in the classroom much beyond the end of their two-year commitment. Randi Weingarten, the president of New York City's United Federation of Teachers, wants more TFA teachers to stay after two years because of the large initial investment. But TFA, supporters say, has never promised its teachers will stay longer.

The TFA says the most reliable data on the comparative effectiveness of corps members comes from a study by Mathematica Policy Research in 2004. Uniquely, the study randomly assigned students within the same schools to teachers both from TFA and traditional certification programmes. It found that students taught by TFA teachers performed slightly better in maths and about the same in reading as those taught by non-TFA novice teachers. But Ms Kopp acknowledges that even the better results shown by one study will not, by themselves, be enough to achieve the TFA's goal: an “excellent education”, one day, for “all children in this nation”.

It will be hard for even a corps of 10,000 teachers to have a large impact in a country that has 3m teachers in public schools alone. But the influence of TFA's alumni, supporters say, is at least as important as the direct impact in the classroom. Placing alumni in other sectors, where they may pioneer changes, is a cornerstone of TFA's strategy. Ms Rhee, the DCPS chancellor, is just one example.

Whether or not they stay in the classroom, the vast majority of corps members are both enraged by the state of the public education system and confident they can help fix it. Every year, Gallup asks the public “Why do we have low educational outcomes in low-income communities?” and offers 20 possible answers. The public's top three responses are “lack of student motivation”, “lack of parental involvement” and “home life issues”. TFA teachers point to “teacher quality”, “principal quality” and “expectations”.

Ultimately, TFA isn't meant to solve the teacher-quality crisis or end teacher shortages or even to create lifelong teachers. It hopes to improve the public education system by convincing young leaders to teach. Critics say the model is wrong, and that the problem lies with parents or pupils or funding, not the teachers. But Michael Podgursky, an economist, says schools can't use home life as an excuse. Andy Rotherham, a former Clinton administration official who now serves on the Virginia Board of Education, is confident TFA will ultimately succeed. “Public education in the United States is...being de-regulated, and that never happens without a fight. What it really boils down to is producer interest versus consumer interest. In the sweep of American history it may take a while, but the consumers ultimately win.”

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Lexington

The school of very hard knocks

Oct 4th 2007
From The Economist print edition

Illustration by Kevin Kallaugher

Inside the mind of a Supreme Court justice

Get article background

HE'S powerful. He's conservative. His daddy was an oil man. He found God and stopped drinking in middle age. The certainty and simplicity of his world view infuriate his many opponents. George Bush? No. The autobiography that is making the American left wobble with rage this week is by Justice Clarence Thomas, the only black member of the Supreme Court. Mr Thomas was paid $1.5m for a memoir that stops dead the moment he joined the court in 1991. About his 16 years working there, he is silent. Perhaps he is planning a second volume. In the meantime, his account of the first 43 years of his life is absorbing and sometimes moving.

Mr Thomas was born in penury and grew up with bare feet and intestinal worms. The man he called “Daddy” was in fact his grandfather (his real father having abandoned him) who was an oil man in the sense that he delivered the stuff in a truck. He could barely read but lived a life of rigid self-discipline, and tried to instil the same values in his grandsons.

When Clarence and his brother Myers arrived, lugging a single grocery bag of possessions each, their grandfather said: “The damn vacation is over.” Clarence thought of the filthy outdoor lavatory he had shared with several other families in a slum in Savannah, and wondered which vacation he meant. Daddy made them work, work, work, at school and in the fields: planting beans, dodging snakes disturbed by the plough, skinning racoons and cleaning fish beneath a light that seemed to draw every insect in south-east Georgia. Daddy taught his grandson self-reliance. Though he found his grandfather's love too tough at the time, he describes him as “the greatest man I have ever known.” His memoir is called “My Grandfather's Son”.

Racially, Mr Thomas began with two handicaps. Not only was he a black boy in the segregated South; he was part of an isolated Creole-speaking community, the Geechees (or Gullahs), dismissed as yokels by other blacks. He pulled himself up by raw intellect and study, with the encouragement of stern nuns. He trained to become a priest, but dropped out when a classmate exulted in the murder of Martin Luther King. “Had the Church been as adamant about ending racism then as it is about ending abortion now,” he writes, his life might have taken a different path. His grandfather wept when he quit the seminary, and threw him out of the house. (They were later reconciled.)

None of these revelations will win Mr Thomas much sympathy. His critics on the left made up their minds long ago. That he is the most conservative judge on the Supreme Court is bad enough. That he is black compounds the offence. His roots are poor, goes the chorus, but he always sides with the rich. His family has suffered from harsh sentencing—he has adopted a great-nephew whose father was jailed for decades for selling crack—yet he fails to strike down such laws. He got into Yale because of racial preferences, but now wants to abolish them. Possibly no other black American is so widely loathed by his own. “Uncle Thomas is a traitor”, read the placards that greet him when he speaks. Al Sharpton has picketed his home. *Ebony* magazine spitefully omits him from its list of the 150 most influential black Americans. A rapper raps: “The white man ain't the devil I promise/ You want to see the devil take a look at Clarence Thomas.”

Mr Thomas is used to brickbats. At his confirmation hearings, Anita Hill, a former employee, accused him of having sexually harassed her several years before. She said he described to her scenes from porn films. He denied it all, and accused Senate Democrats of carrying out “a high-tech lynching for uppity blacks who in any way deign to think for themselves.” He was confirmed by the slimmest of margins. Both he and Ms Hill stand by their stories. No one else knows which of them committed perjury. Television coverage of Mr Thomas's book has focused like a cheap stage-light on this episode, though Mr Thomas has little new to say about it, save that he is still angry.

Critics and counter-criticism

But just as Bill Clinton's presidency was about more than stained dresses, so Mr Thomas's story is about more than Long Dong Silver. There are two substantive criticisms of him. One is that he is not clever enough to sit on the Supreme Court. He seldom speaks during public hearings, and his doubters whisper that he blindly follows Justice Antonin Scalia. But another recent book, Jan Crawford Greenburg's excellent “Supreme Conflict”, reveals that behind closed doors he is apparently cogent and forceful. A dissent he wrote for his third case on the court prompted both Mr Scalia and the then chief justice, William Rehnquist, to change their minds.

The second carp about Mr Thomas is that he is cruel. Rather than seeking justice, he coldly applies the law as it is written. To conservatives, that is his chief virtue. Judges who conjure up rights that are not mentioned in the constitution—such as the right to an abortion created by *Roe v Wade* in 1973—undermine the rule of law. He rules in favour of the rich if, and only if, that is what the constitution requires. He rules against racial preferences because he thinks the equal protection clause means what it says.

Mr Thomas would reverse not only *Roe v Wade* but also any ruling he deems ungrounded in the constitution's text. That puts him in a minority of one on the nine-strong bench; all the other justices like to pay at least some heed to precedent. But he does not care. It is up to lawmakers to make laws, he reckons. If the voters don't want change, politicians should persuade them, not just keep their heads down and hope that unelected judges will make the hard choices for them. His message to politicians echoes the simple homilies his grandfather taught him. Do your job. Take responsibility. No wonder he is so unpopular. But the court would be poorer without him.

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Latin America and the United States

Commerce between friends and foes

Oct 4th 2007 | LIMA AND MEXICO CITY
From The Economist print edition

The United States may finally ratify a trade deal with Peru. But pan-American trade diplomacy remains a mess

IN HIS first term as Peru's president, in the 1980s, Alan García was a firm believer in protectionism, banning the import of foreign cars and even of Chilean wine. But since coming to office again last year he has embraced free trade with a passion bordering on mania. “More trade and more investment [means] less migration, less poverty and less environmental destruction,” he told a meeting in Lima last month convened by the World Trade Organisation (WTO). “You might resign yourself to just having a free-trade agreement with the United States, but for me it's not enough,” he told his audience, ordering his harried trade minister to secure similar deals with a score of other countries.

That Mr García was so pumped up was perhaps because at long last Peru's trade deal with the United States, negotiated 18 months ago, looks close to ratification by a hitherto reluctant American Congress. On September 27th the administration sent a bill to Congress after a majority of the House Ways and Means Committee and the Senate Finance Committee indicated they would back it. Though upsets are still possible, supporters reckon the bill will be approved within weeks. But for free-traders, that is cause for only the faintest cheer.

The benefits to Peru seem clear. Mr García, who when a candidate was sceptical of the deal, now says that it could add an additional percentage point to economic growth (which reached 8% last year). That is mainly because it provides investors with greater security. Peru's industrialists' association reckons that it could prompt an extra $9 billion in industrial investment in 2008 and 2009 alone.

Opponents worry that farmers, especially of maize, cotton and wheat, will struggle to compete with their subsidised counterparts in the United States. They also fret that American companies will try to take out patents on Amazonian plants.

Free-traders have other worries. A decade ago, the United States and 33 countries in Latin America and the Caribbean hoped to negotiate an all-embracing Free Trade Area of the Americas (FTAA). But the mood has changed. The Democrats, who won control of the American Congress last November, are

mistrustful of trade agreements, reflecting widespread fears that globalisation has made jobs more insecure in the United States. Mercosur, the trade block led by Brazil, backed away from an FTAA in favour of the Doha round of WTO talks, but these have stalled too. All this comes as some governments in Latin America, led by Venezuela's Hugo Chávez, are turning their backs on open trade.

Others have negotiated bilateral free-trade agreements (FTAs) with the United States. But George Bush's administration has struggled to persuade Congress to ratify them: even before the Democrats took control, the Central American Free Trade Agreement (known as CAFTA-DR) passed by just two votes; as well as Peru, deals with Panama and Colombia (and South Korea) still await approval.

So Latin American politicians, such as Mr García, who see trade as an engine of growth, find themselves caught between American indifference and a resurgent, anti-trade left at home. When they negotiate bilateral FTAs, they are in a much weaker position than they would have been when gathered together in an FTAA.

Even so, the Democrats have insisted on changing the agreements. In May they struck a deal with the administration under which the FTAs would have to include clauses to strengthen labour rights and the environment (see article), while slightly loosening intellectual-property protection (giving more flexibility for generic medicines). The Democrats say this was the only way to restore bipartisan consensus on trade. Some economists note that since countries such as Peru already subscribe to many of these standards, in theory at least, their formal incorporation is no big deal.

Even so, only a minority of Democrats are likely to vote for any of the FTAs. Peter Hakim of the Inter-American Dialogue, a think-tank in Washington DC, reckons that at most about 70 of the 232 Democrats in the House of Representatives might vote for the Peru FTA. The agreement with Panama was supposed to be next in line. But the Bush administration has balked over the recent choice to head Panama's parliament of a politician whom it accuses of killing an American in 1992.

The FTA with Colombia faces even bigger obstacles. The Democratic leadership in the House has refused to back it, arguing that Colombia's government needs to do more to prevent the killing of trade unionists and to punish officials linked to right-wing paramilitaries. That was a slap in the face for Álvaro Uribe, Colombia's president, who has been Mr Bush's most loyal ally in Latin America. Colombian officials argue that their efforts to strengthen the rule of law in the face of violence from drug traffickers, guerrillas and former paramilitaries will be undermined by failure to approve an FTA.

This is a powerful point and an objection to the whole structure of trade agreements that is now evolving in Latin America. If the agreements with Peru and Panama are approved, the effect would be to divert trade and investment from Colombia. A recent study by EAFIT, a university in Medellín, and the University of Antioquia found that if the Colombia FTA is not approved and the others are, Colombia's GDP would be 2.2% smaller and 400,000 jobs would be lost.

Some Democrats, at least, recognise that this would be a perverse outcome. Mr Hakim reckons there is a chance the Colombia agreement could be ratified next year—but only if Mr Uribe's government takes further steps to protect trade unionists, and these are seen to be working.

The United States' hard-nosed approach to trade is winning few friends in Latin America. That may become apparent in Costa Rica, which is holding a referendum on October 7th on whether to ratify CAFTA-DR. Polls suggest the result will be close, but opponents appear to have momentum. They recently assembled more than 100,000 protestors in San José, the capital. Although Oscar Arias, the president, insists the accord is vital to his country's future, his government may have overplayed its hand. Last month one of his vice-presidents resigned after the leaking of a memo in which he advocated scare tactics such as painting opponents as allies of Mr Chávez. Some are—but others merely think CAFTA-DR a bad deal, especially in its intellectual-property clauses.

If the American Congress does ratify the pending FTAs, turning its back on CAFTA-DR could cause Costa Rica to lose jobs—a fate that may also await Bolivia and Ecuador. This whole mess underlines that bilateral deals are a third-best option after the Doha Round or the FTAA. But for those Latin American countries that are ambitious to expand their share of the biggest market for manufactured exports, they are the only game in town.

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Peru

Trade, timber and tribes

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From The Economist print edition

The Democrats in the United States take on the loggers in Peru

SEPAHUA, a ramshackle town on the edge of Peru's Amazon jungle, nestles in a pocket on the map where a river of the same name flows into the Urubamba. That pocket denotes a tiny patch of legally loggable land sandwiched between four natural reserves, all rich in mahogany and accessible from the town. “Boundaries are on maps,” says a local logger, “maps are only in Lima,” the capital.

In 2001 the government, egged on by WWF, a green group, tried to regulate logging in the relatively small part of the Peruvian Amazon where this is allowed. It abolished the previous system of annual contracts. Instead, it auctioned 40-year concessions to areas ruled off on a map, with the right to log 5% of the area each year. The aim was to encourage strict management plans and sustainable extraction.

A recent study using satellite data by America's Carnegie Institution found that this policy did limit damage to the forest, at least until 2005. But greens on the ground say that the system gives loggers an incentive to overestimate the number of valuable trees in their patch. Some have filled their puffed-up yearly allowance with mahogany taken from natural reserves and from Indian land. A report by the forestry regulator found that only 22 of the 79 concessions it investigated contained as much mahogany as the loggers claim.

As loggers venture into reserves such as Alto Purús, they have clashed with isolated Indian groups, with killings on both sides. Last month government ecologists spotted from the air 21 members of a hitherto uncontacted tribe on the banks of the Río de las Piedras. Peru's Amazon Indian association reckons there are still 15 such groups.

Greens say that under the new system, just like the old, much of the timber exported from Peru (officially $200m last year) is cut illegally, with the connivance of the authorities. They have won the support of the Democrats in the American Congress, who insisted on inserting a “timber annexe” in the free-trade agreement with Peru. This gives Peru 18 months to hire more forestry inspectors, set up a stronger forestry regulator and stiffen penalties for illegal logging. It will also allow American officials to halt suspicious shipments at the border, and to visit Peru to see where they come from.

Few in Peru welcome such intrusion. Will it succeed in reducing the trade in illegal mahogany? Some reckon that better enforcement will indeed help to preserve the forest—though where Peru will get the funds for this is not clear.

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Ecuador

Correa's victory

Oct 4th 2007 | QUITO
From The Economist print edition

A mandate for “21st century socialism”

Get article background

HE CALLED it the “mother of all battles” and Rafael Correa, Ecuador's new young president, appears to have won it. According to an unofficial count of the results of an election on September 30th for a Constituent Assembly, Mr Correa's supporters, grouped in a new outfit called Acuerdo País (“Agreement for the country”), won some 70 or more of the 130 seats. That gives the president a clear mandate to write a new constitution reflecting the “21st century socialism” he espouses.

Just what this will entail remains unclear. On the one hand, Mr Correa says the assembly has the power to dissolve the Congress, dominated by his opponents in the traditional parties, which was elected at the same time as him last year. This is the same modus operandi deployed by Venezuela's Hugo Chávez, with whom Mr Correa is friendly.

But on the other hand, Mr Correa has recently stressed that his intentions are not authoritarian and that he doesn't want to copy Mr Chávez's project of abolishing presidential term limits. Socialism is a “principle not a regime”, he said. He added that he was willing to hold friendly discussions with private business about his plans for a “solidarity economy”. The signs are that his constitutional plans will involve an increase in presidential powers and in the role of the state in the economy—but by how much?

The uncertainty partly stems from the president's mercurial personality: he has flip-flopped between belligerence and moderation over the past year. It is also because Acuerdo País is a heterogeneous lot. Some of Mr Correa's advisers would be happy to see him hew closer to the *chavista* path; others are moderate centre-leftists.

What Mr Correa may already have achieved is a decisive break in the pattern of Ecuador's politics. Three presidents have failed to finish their term since 1996. Real power has lain with two parties, the right-wing Social Christians, based in Guayaquil, the main port, and the Democratic Left, strong in Quito, the capital. Between them these two parties appear to have won just five seats in the assembly.

Misgovernment by Congress has caused Ecuador's economy to languish: at least 750,000 people migrated after bank collapses triggered a slump in 1999-2000. Mr Correa, an economist who studied at the Catholic University of Louvain in Belgium, is popular because he rails against the “partyocracy” and the bankers that he claims have bilked the country.

Since Mr Correa took office in January, he has increased subsidies and social spending. But economic growth and investment are both slowing. He says he has not yet had time to transform his country. He now has the power to do so. But time may be short: ethnically and geographically diverse, Ecuador has rarely united around anyone for long.

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Canada

Playground politics

Oct 4th 2007 | OTTAWA
From The Economist print edition

Ontario debates religion and schools

HOW far should the majority go to accommodate the religion and culture of recent immigrants? Quite a long way, has usually been the answer in Canada, which prides itself on its multiculturalism. But John Tory, the happily named leader of the Progressive Conservative party in Ontario, has found that there are limits even to Canadian tolerance.

Mr Tory seemed to have a good chance of kicking out the ruling Liberals in a provincial election on October 10th. But his platform includes a plan that the provincial government should extend the same financial support that it has long given Roman Catholic schools to religious schools of all denominations. “Fairness dictates that we should fund all faiths, or none at all,” he said. Withdrawing support from Catholics, who account for a third of the population and whose schools won a constitutional guarantee of financing 140 years ago, would have been divisive. But Mr Tory's impeccably logical alternative turned out to be equally so.

His opponents saw a cynical attempt to woo the province's large ethnic-minority vote (44% of residents in Toronto are foreign-born). Mr Tory countered that half a dozen other provinces already give some money to religious schools. But many voters seem worried that the plan might weaken—and divert funds from—the public-school system, loosening the glue that bonds the new arrivals to Canada. Ontarians fear that further school segregation by religion “would exacerbate centrifugal forces in society,” says Donna Dasko of Environics Research, a polling firm.

Islamophobia reared its head, too. The 2001 census found that Muslims made up just 3% of the population, but that is double the proportion of ten years before. Some opinion pollsters detected fears among a large minority of respondents that taxpayer-funded *madrassas* would train terrorists. But there seems to be little voter appetite for paying for Hindu, Jewish, Pentecostal or Sikh schools either.

This week Mr Tory backed away from the idea, promising a free vote in the legislature if he wins. That looks increasingly unlikely. The issue has been a gift for Dalton McGuinty, the Liberal premier (who attended a Catholic school). It has diverted attention from a big tax increase that broke a promise he made in the 2003 election.

The broader question raised by this not very edifying debate is what role religion should play in public life. On the whole, Canadians reckon it should be a private matter: bible-thumping politicians have rarely been popular. Maybe Mr Tory should have proposed that Ontario follow Quebec (where Catholics are a large majority) and (strongly Protestant) Newfoundland, which have both approved constitutional amendments to make their school systems entirely secular.

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Mexico

Reflections from the ranch

Oct 4th 2007 | MEXICO CITY
From The Economist print edition

Vicente Fox remembers

ANYONE looking to understand Vicente Fox's shortcomings as Mexico's president from 2000 to 2006 could do no better than read his memoirs. In “Revolution of Hope”, a ghost-written volume published in English in the United States (but oddly not yet in Mexico in Spanish), Mr Fox concedes that his critics may have been right that he was “too naive” for political infighting, “not a skill I aspire to learn”. He was, he says, “at peace” from the day in 2000 he won the presidency, overturning seven decades of one-party rule.

Mr Fox, a farmer and former Coca-Cola manager, was indeed an excellent presidential candidate, and his victory marked his country's final transition to democracy. Sadly, he achieved little thereafter, although he met a lot of world leaders whose names are duly dropped, weighted with superlatives. Tony Blair is the most persuasive man on earth. As for George Bush, Mr Fox clearly liked him (though not some of his policies), praising his focus, warmth and broken Spanish. But Mr Fox also deftly puts down Mr Bush as a “windshield cowboy”, more comfortable driving a 4x4 around his Crawford ranch than riding a horse. When Mr Fox, who never shed his cowboy boots even when dressed in a business suit, offered his big palomino horse, “George” demurred.

EPA

He was a better cowboy than George Bush

Some of the strongest passages concern Mr Fox's love for his own ranch. (Mexico's Congress last month launched an investigation into its expensive refurbishment.) He also has a few strong beliefs: free trade and microcredit are both good; America needs to reform its immigration policy; democracy is important, particularly to Mexico. But he sheds little light on the battles of his presidency, such as his opposition to the Iraq war, or his ill-conceived attempt to block the presidential candidacy of Andrés Manuel López Obrador, a leftist opponent.

Coming from a man who seemed to promise so much, Mr Fox's book, like his presidency, is oddly lightweight. Its aim seems to be to secure work on the conference circuit rather than to illuminate his years in power.

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Myanmar

Shouting across the barbed wire

Oct 4th 2007 | BANGKOK
From The Economist print edition

EPA

Myanmar's neighbours are talking tough but doing little to show their disapproval of the killings in Myanmar

Get article background

IBRAHIM GAMBARI, the United Nations' special envoy to Myanmar, kept everyone guessing after his four-day visit to seek an end to its military regime's harsh crackdown on protesters. On October 2nd he flew out, having met the regime's leaders in their remote new capital, Naypyidaw, and also Aung San Suu Kyi, the pro-democracy leader in detention in the main city, Yangon. The envoy was due to report to the UN secretary-general, Ban Ki-moon, on his return to New York. Mr Ban had already deflated hopes for an immediate breakthrough by saying of the envoy's mission: “You cannot call it a success.”

He did, however, confirm that Mr Gambari will pay another visit to Myanmar in November. And state television had reported that General Than Shwe, who heads the junta, had told him he would talk to Miss Suu Kyi, on certain conditions: that she stopped being “obstructive” and backing sanctions. So there is a faint hope that international pressure might indeed make the regime open a dialogue with the pro-democracy movement, leading ultimately to a peaceful settlement. That, however, still seems a long way off, even were Miss Suu Kyi to agree to general's terms for talks. During Mr Gambari's visit, the regime continued making large-scale arrests of suspected pro-democracy campaigners; and the regime defiantly blamed meddling foreigners for instigating the protests. It hardly seemed ready to compromise. In the past, talks with Miss Suu Kyi have been used as a sop to placate international opinion.

As tens of thousands of Buddhist monks took to the streets late last month, it was hoped that the government would hesitate to crack down too hard on them, because of the reverence that the clergy command from ordinary Burmese. However, the troops and riot police sent into the streets on September 24th quickly demonstrated their ruthlessness. Monks were beaten, arrested and in some cases shot or bludgeoned to death. By the weekend, with the last signs of resistance quashed and the country's internet connections cut off, the flood of news and pictures coming out of the country had become a trickle. But one image seen around the globe, of the battered body of a young monk, face down in a ditch, said it all.

Large numbers of monks have been carted off to unknown places of detention. Perhaps thousands are being held at the Government Technical Institute, north of Yangon, though some were freed on October 3rd. State-controlled media have admitted to only ten deaths since the protests began, claiming they were handled “with care, using the least possible force”. Diplomats believe there may have been hundreds of deaths. But, as with the crackdown on the student-led protests of 1988, the toll may never be known.

By the middle of this week, Yangon's streets were quiet. Fewer troops were patrolling, a night-time curfew had been reduced by two hours and access to the golden Shwedagon Pagoda—the country's holiest shrine and the rallying-point of the monks' protests—was restored. The junta seemed confident it had beaten the life out of the protests, for now at least.

Less is known about the situation in other towns that had big, monk-led protests. The UN's World Food Programme (WFP) said that army chiefs in Mandalay briefly restricted its much-needed food supplies (see article). By midweek, the restrictions had been lifted, though the WFP said it was running out of money and was thus unable to reach more than a fraction of the 1.6m Burmese it is trying to feed.

The worldwide dissemination of graphic images of the violence has forced many of Myanmar's Asian neighbours to go beyond their usual stance of non-interference in other countries' affairs. Wen Jiabao, the prime minister of China—Myanmar's largest supplier of imports and its third-largest export market—expressed deep concern about the situation and urged efforts to “promote domestic reconciliation and achieve democracy and development.” Japan said it might cut aid to Myanmar after the shooting of a Japanese journalist by a soldier during the Yangon protests. The feeblest response among those countries engaged with Myanmar came from India. Its ministers' vague talk about the need for peaceful dialogue was undercut by the new army chief, who said India wanted to maintain its close relationship with the regime.

George Yeo, Singapore's foreign minister, claimed this week that the Association of South-East Asian Nations (ASEAN) has “very little leverage” over Myanmar's regime, which was admitted to the regional body in 1997 in the hope that constructive engagement might achieve what Western sanctions had not. “We can't do what the big powers can do in terms of trade embargo or freezing bank accounts,” said Mr Yeo. For “can't”, read “won't”. There is plenty that ASEAN could do. Some regime leaders are thought to have bank accounts in Singapore, which could indeed be frozen. Thailand is by far the largest buyer of Burmese exports (principally gas). Thailand and Singapore are second and third behind China in supplying the country.

So, some well-chosen sanctions, or even a credible threat to consider them, might have an impact. The West's sanctions on Myanmar have failed in part because the East has enthusiastically filled the breach. At the very least, suggested Mr Gambari's predecessor, Razali Ismail, ASEAN could start by insisting on sending its own envoy to Myanmar. ASEAN has paid a high price for admitting the country and this seems the least it could do.

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Myanmar

Misery piled upon misery

Oct 4th 2007 | BANGKOK
From The Economist print edition

The regime's incompetence has left the Burmese starving and sick

Get article background

THE drastic increase in fuel prices last month, which made life even more difficult for ordinary Burmese and set off the latest round of protests, was only the latest proof of the junta's catastrophic economic incompetence. After seizing power in 1962, the regime pursued the “Burmese Way to Socialism”—isolationism combined with a military takeover of businesses. A capricious decision to withdraw most banknotes in late 1987 sparked massive protests the next year, which were bloodily quelled. This triggered Western sanctions and the suspension of loans from the World Bank and other multilateral agencies. But any economic damage done by these is as nothing compared with that wreaked by the junta's continued repression, corruption and economic cackhandedness.

It is often noted that before 1962 the then Burma was the region's rice-bowl. It is less well known that the country still produces a rice surplus. However, the regime's travel restrictions, its rampant corruption and the lack of decent roads mean that many Burmese still go hungry. The situation is worst in the border areas where Myanmar's ethnic minorities live. Most rice merchants are military men with no interest in feeding minorities who might rise up against them. Farmers trying to take produce to market are stopped at army checkpoints by bribe-hunting officers. The WFP says that about a third of Burmese under-fives are “chronically malnourished”, one of the world's highest rates.

EPA

The telephone never rings

The regime is reckoned to spend less than 2% of its budget on health care, compared with over 40% on the armed forces. Infectious diseases are as widespread as in poor African countries. A report in July from Berkeley and Johns Hopkins universities in America said Myanmar had one of the world's highest rates of tuberculosis and that drug-resistant forms of both tuberculosis and malaria were spreading. HIV infection has broken out of high-risk groups and become a general epidemic. But restrictions on aid workers' movements forced the Global Fund to Fight AIDS, Tuberculosis and Malaria to pull out in 2005. The International Committee of the Red Cross, often the last NGO to leave, has also had to curtail its operations.

To starvation and sickness are added the trials of forced labour, sometimes as porters for the army in mine-infested areas, and reports of the army's recruiting child soldiers. The economy is growing at perhaps 3-4% but much of the growth comes from the exploitation of natural resources—from gas to gemstones—whose proceeds mainly benefit the regime's pampered families.

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Sri Lanka's war

The northern front

Oct 4th 2007 | OMANTHAI AND VAVUNIYA
From The Economist print edition

The army thinks it can win. It is wrong

Get article background

FROM the line of dusty travellers leaving the Tamil Tigers' heartland in northern Sri Lanka, young men are strikingly absent. The people trudging out of rebel territory, across a strip of scrubby ground dotted with bundles of barbed wire and gun-slung soldiers, say securing exit passes from the rebels has become increasingly tough. For the young, it is all but impossible. As far as the Tigers are concerned, they are potential fighters.

The rebels want to keep the young and fit in their stronghold, a mini-state run with thuggish ruthlessness. Since 1983, the Liberation Tigers of Tamil Eelam have fought for an independent “homeland” in the east and north for the island's Tamil minority. In July the Sri Lankan army declared it had cleared the eastern part for the first time in 14 years. Now its sights are on the north. In his heavily fortified headquarters in the capital Colombo, the army chief, General Sarath Fonseka, says he expects to chase the Tigers from the north in a year, “maybe less”.

This is more than a commander's bravado. After the army's triumph in the east, subsequent victories suggest the Tigers' strength is diminished. In early September the army cleared an area just south of their heartland, capturing a Tiger naval base purportedly used to receive smuggled weapons. Days later it sank three ships it said were ferrying light aircraft and a bullet-proof car for the Tigers' chieftain, Velupillai Prabhakaran. In eastern Sri Lanka some Tamils express surprise, and sometimes disenchantment, that the Tigers' roar has been more muffled of late.

If the army did win the north while holding the east it would constitute a huge and unprecedented victory. Its last big push into the area, in the late 1990s, ended with hundreds of dead soldiers and a humiliating retreat. In the east, which has a mixed population of Tamils, Sinhalese and Muslims, the rebels' hold was patchy and the army was helped by the defection in 2004 of the Tigers' commander in the region, known as Colonel Karuna. The Tigers hold the Tamil north in a much tighter grip. And the army has fewer soldiers than it would like for its northern campaign, because it is busy securing the east.

Days after the government celebrated its latest victories in the eastern port town of Trincomalee last month, suspected Tigers bombed a bus in the area, killing the driver and wounding several passengers. Though such incidents in the east have decreased, they suggest that the Tigers remain a force to be reckoned with. In the north, on the margins of their fief, there are areas where it is unclear quite who is in

control: the army or the rebels.

Even a northern victory, momentous as it would be, would not bring an end to Sri Lanka's conflict. That will not come without a political solution, giving some measure of autonomy to the island's Tamils who have suffered discrimination from the Sinhalese majority more or less since independence.

A cross-party group of politicians has made some progress on this front, agreeing that the island should be devolved at the provincial level—an improvement on an earlier government proposal for district-level devolution. But last month the defence minister, Gotabhaya Rajapakse (brother of the president, Mahinda Rajapakse), made it clear where the government's priorities lay. A political solution, he said, would be impossible without first crushing the Tigers. This dashed any faint hope that the ceasefire agreement the government and the Tigers signed in 2002, and which is still notionally in force, might yet be revived.

In the east, meanwhile, the government has an opportunity to show Tamils they are better-off under the government than they were under the rebels. But its commitment to this goal is questionable. In a Trincomalee town hall with views of the glittering Indian Ocean, more than 80 families sleep on a concrete floor amid battered cardboard boxes of possessions. They have lived here for more than a year, since they were shelled out of their homes in nearby Sampur, a former Tiger stronghold; thousands more of their fellow townspeople languish in camps outside the town. Though few of them seem to know it, they are unlikely to return home: Sampur has been turned into a no-go high-security zone for the army.

The government faces other challenges if it is to pull off victory in the north. People in Colombo, for whom the war is a rather distant affair, may not have heard any bombs lately. But they complain about rocketing inflation, and political support for President Rajapakse's government is ebbing. Dogged by allegations of incompetence and corruption, it is expected to be further weakened when it presents its budget in November. In last year's, military expenses surged by 44%. Another big rise will increase pressure to show that all this spending is achieving something.

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Pakistan's presidential election

Down to the wire

Oct 4th 2007 | LAHORE
From The Economist print edition

Even a rigged vote in a depleted electoral college can be a cliff-hanger

Get article background

HE ALREADY had the numbers, but that was not enough. General Pervez Musharraf enjoyed the parliamentary majority he needed to be re-elected president of Pakistan on October 6th as scheduled. But without an agreement with Benazir Bhutto, a former prime minister and leader of Pakistan's most popular political party, it would have been a hollow victory. As *The Economist* went to press, the final details of such a deal were being hammered out. Even so, brinkmanship on both sides and a legal tangle in the Supreme Court meant that the general's re-election was still far from a done deal.

General Musharraf is embroiled in constitutional and political battles that hinge on prickly judges, street agitation and fine points of law. Benazir Bhutto, the one person who can bail him out, has played hard to get. Twice-elected to—and twice-ousted from—the prime minister's office, she has been in exile sheltering from a sheaf of corruption charges. She has been negotiating with General Musharraf for the past two years. She wanted amnesty from prosecution for herself and others, a free and fair election and the right to be prime minister a third time (at present banned under the Musharraf-mangled constitution). In return she says she would accept (but not vote for) him as a president, provided he resigns his post as army chief.

AFP

Down but not out

General Musharraf had been stalling. His backers in the ruling Pakistan Muslim League (Q) party were loth to countenance any deal with their sworn political enemy. But if no deal were concluded before the presidential elections, Miss Bhutto's People's Party, which won nearly 29% of the vote in the last general elections in 2002, would have resigned from the federal and provincial parliaments that form the electoral college. Earlier this week more than 160 members of other opposition parties had resigned from the parliaments in protest at General Musharraf's attempt to have himself elected while still in uniform. Had Miss Bhutto's supporters followed them, the election would have appeared a wholly illegitimate farce.

Miss Bhutto's dalliance with General Musharraf has been controversial. It has allowed her nemesis, Nawaz Sharif, another former prime minister, to present himself implausibly as the opposition's democrat, having no truck with dictators. Last month, on his return from exile to Pakistan, he was presented with corruption charges and swiftly packed off again.

Agreement with Miss Bhutto, however, will not remove every obstacle between General Musharraf and re-election. There remained still the risk of a last-minute spanner thrown in the works by the Supreme Court. The court became the focal point of popular agitation in July, when it reinstated its maverick chief justice, Iftikhar Chaudhry, whom General Musharraf had sacked in March. The court has since crossed swords with General Musharraf on several occasions.

On September 28th the Supreme Court, in a six-three judgment, did however reject a clutch of petitions against General Musharraf's bid to be re-elected while still in his army chief's uniform. The government heaved a sigh of relief and promptly nominated the general to the presidency. But the reprieve was short-lived. Against the backdrop of popular disenchantment with the pro-Musharraf decision, the court decided on October 2nd to hear again constitutional objections to the chief election commissioner's acceptance of the general's nomination papers.

In theory, the court could now delay the presidential election until judgment day, whenever that may be;

or, even worse from General Musharraf's point of view, prolong the hearings but allow the presidential election to go ahead. This would throw a deep shadow over his presidency until it gave its verdict. He has pledged to doff his uniform after being re-elected president. To be a civilian president with the Supreme Court's sword dangling over his head would be unnerving. “That would amount to blackmail,” says a presidential aide. “We won't accept it.” Should the court make such a decision while General Musharraf is still army chief, that presumably means martial law, however unpopular at home and abroad it may be.

On October 2nd General Musharraf promoted the head of the powerful Inter-Services Intelligence (ISI), General Ashfaq Kayani, to be his deputy as army chief, and his designated successor in that job when he steps down as promised. He also promoted five other generals. This was supposed to signal his readiness to return the army to barracks and usher in a transition to greater democracy. But no one was fooled. The promotions are all well-deserved but there is no doubt that he has placed loyalists in all important positions before retiring as army chief.

Unfortunately, the idea that even as a civilian he will retain powerful influence over the army is exactly what provokes the opposition. So General Musharraf's fate hangs in the balance. The Supreme Court detests his overbearing manner but still has not mustered the courage to defy him and risk martial law. The opposition of right-wing mullahs and conservative politicians hate him for his pro-Western stance but cannot inspire a popular revolt against him. Meanwhile, the West worries about life both with and without General Musharraf. If he survives by dint of the gun, Pakistanis will blame the West for propping him up and veer towards the Islamists, which will undermine the “war against terror”. If he is ousted, a free-for-all-election might well produce a badly fractured electoral verdict, and do similar damage to the struggle against Islamist extremism.

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Australia's farmers

Dried up, washed out, fed up

Oct 4th 2007 | GULARGAMBONE
From The Economist print edition

An inaccurate weather forecast brings disaster for many

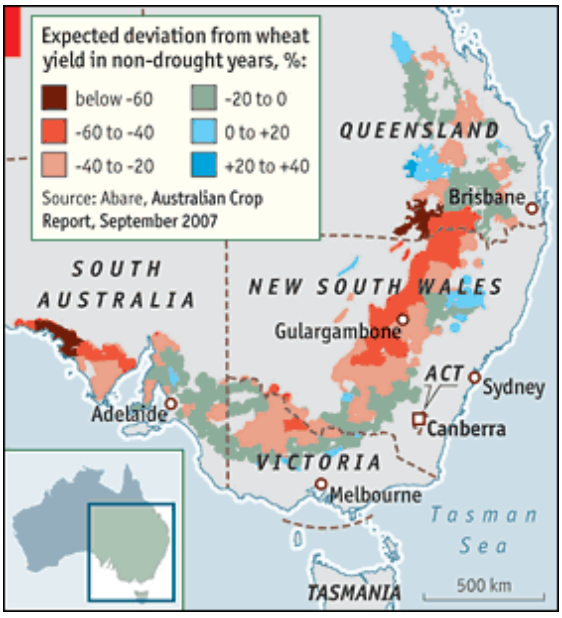
AFP

You need a dry sense of humour

WHEN rains fell in May after 11 dry years in a row, Bruce Crafter borrowed from his bank to sow a wheat crop on the family farm where he grew up in western Victoria. Like thousands of Australian farmers who have watched their livelihoods wither away under the country's worst drought in a century, Mr Crafter was encouraged by forecasts of follow-up spring rains in September. He sold one-third of his expected bumper crop on the futures market. But the rains never arrived, and the crops that promised salvation have failed. With no intended irony, Mr Crafter says: “We've been washed out.”

“Wash-out” is the term farmers are using to describe the contracts they can no longer fulfil. Australia is one of the world's biggest wheat exporters. The crop underpins the country's outback farming belt. After recent glitches to wheat supplies in North America and Europe, hopes were riding on the Australian crop, due for harvest by December, to help fill a gap in global demand. The hopes now seem forlorn. In September, the Australian Bureau of Agricultural and Resource Economics, a government research agency, cut its forecast of Australia's wheat production this year to 15.5m tonnes, one-third below its June forecast. The failure of crucial spring rains since then means production is likely to be even less.

The farming crisis is so bad that the federal government in late September announced A$1.1 billion ($1 billion) in drought aid. It included payments of A$150,000 each to the most debt-ridden of Australia's 130,000 farmers to leave their land. Some city Australians enjoying the jobs, money and good times of a booming market economy were quick to decry the largesse. Yet the drought, which has driven farmers to despair, and some to suicide, is now pushing up food prices in suburban supermarkets. Its impact cut three-quarters of a percentage point off Australia's growth rate in 2006-07.



The calamity is worst in New South Wales (NSW), the most populous state, where wheat-production forecasts for 2007-08 have been almost halved. Some farmers there face ruin. After gambling on the Australian Bureau of Meteorology's rain outlook, they sold their crops forward. Meanwhile, wheat prices

doubled. With little crop to deliver in December, those farmers now face the grim prospect of having to pay the difference in prices.

Mr Crafter's brother Ian left farming 23 years ago to set up a business that builds livestock yards Australia-wide; it turns over up to A$7m a year. He reckons the vagaries of dry weather and global markets make this drought the worst he has seen: “We need biblical-style rainfall.” With fewer livestock to pen, his business too has been hit. Graham Peart, who owns a sheep stud at Gulargambone, a pioneering-era village where it has not rained for six years, estimates farmers have cut stock numbers by one-third to make way for an illusory bonanza from crops.

Farmers are now asking whether much of the outback that supported their forebears can still sustain them. A report this week by the Commonwealth Scientific and Industrial Research Organisation, a government body, gave little hope. It predicted less rain, more droughts and temperature rises of more than 1° C by 2030. But Mr Peart quotes a friend who has stopped believing in climate change, because “It hasn't rained in eight years.”

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The Koreas

It'll cost you

Oct 4th 2007 | SEOUL
From The Economist print edition

Everybody claims a breakthrough with North Korea. This sounds familiar

BRINGING his own food, and accompanied by 300 business, political and cultural figures—but excluding the international press—President Roh Moo-hyun of South Korea drove to Pyongyang on October 2nd to call upon North Korea's Kim Jong Il. At the heavily-armed border, which Bill Clinton once described as "the world's scariest place", Mr Roh got out of his limousine to cross on foot—a step, he wanted everyone to know, that symbolised a desire for peace and reconciliation between the two estranged sides of a bloody civil war that remains unresolved more than 50 years after it ground to a halt.

It was only the second-ever meeting between leaders of the two countries, and Mr Roh's gambit was aimed at the history books. He wanted to salvage an ineffectual presidency, which ends in December, by asking Mr Kim to reduce tensions on the peninsula in return for economy-transforming aid and investment. Mr Roh's approach has led to divisions even among his own advisers. Some, such as the unification minister, Lee Jae-joung—described by one Western diplomat as an "unguided missile"—are gung-ho for reconciliation and are prepared to overlook a lot of Mr Kim's unpleasantness.

EPA

The end of the line for Kim?

Others despise the repressive regime of Mr Kim, and know that behind him lies a trail of broken promises. To offer too much now might also undermine the multilateral "six-party" process taking place in parallel, in which North Korea is being offered measured aid in return for clear steps towards dismantling its nuclear capabilities.

Though this summit drew the opaque Mr Kim out from the shadows somewhat, he remains hard to read. During the first summit, in 2000, when he met Mr Roh's predecessor, Kim Dae-jung, Mr Kim was all bear-hugs and smiles. That meeting generated mass euphoria in North and South, but little of substance came of it—not even Mr Kim's promised return visit to Seoul. It later turned out that $500m had been paid to Mr Kim just for the audience.

This week the befuddled looks of farmers as Mr Roh's presidential cavalcade swept up the highway to Pyongyang suggested that Mr Kim had not let all his compatriots in on the historic moment, one for which Mr Roh has begged for years. Though a handpicked crowd in the capital gave a joyous reception, waving artificial bunches of Kimjongilia, a type of begonia that is the national flower, Mr Kim himself was stiff and tight-lipped. To many of his countrymen, he will have looked on television like an emperor receiving tribute. But many outsiders once again wondered about the health of the pallid, pot-bellied 65-year-old. Mr Kim is known to have had heart problems, and some intelligence analysts recently have claimed to see the early signs of senile dementia—though this is mere conjecture.

From what can be gleaned of their substance, talks between the two leaders on October 3rd only emphasised the distance still to travel. Mr Kim may be willing to squeeze the outside world for aid—but on his terms. So Mr Roh's offer of what amounted to a Marshall Plan to transform North Korea's economy in pursuit of Chinese-style liberalisation met with blank dismissal. Mr Kim does not even like a showcase industrial park at Kaesong, where South Korean manufacturers employ cheap North Korean labour, to be described as a model of successful "reform". Once again, Mr Kim showed how he puts his own survival over that of the North Koreans he brutalises.

Yet a joint agreement was announced on October 4th, something Mr Roh will be able to take home with relief. Gone were his hopes for great involvement in the North, but there was agreement to allow freight trains into Kaesong. There was a recommitment to help families divided by the civil war to meet (though a

word from Mr Kim is all it would take to solve that sad problem). Talks will be sought with America and China to put a formal end to the civil war (though peace on the peninsula, these countries are likely to argue, can only come after its denuclearisation). Steps were promised (as, fruitlessly, they were at the 2000 summit) to reduce military tensions: defence ministers would meet, while a disputed western maritime area would see its fisheries jointly mined.

Promising as all this sounds, much of it merely repeats earlier promises. In the long run, Mr Kim has never really seen his interests as best served by closer relations with the South. They might lead, eventually, to reunification and hence to his dynasty's extinction. China, Japan, Russia and America, the other parties in the six-party talks, may loathe his regime, but they are in effect helping to prop it up.

Peace dividend

As Mr Roh struggled to secure his piece of paper in Pyongyang, the Chinese government this week declared a breakthrough in those talks as well. Almost a year after North Korea exploded a nuclear bomb, the Chinese said the country had agreed to disable its main nuclear reactor and reprocessing plant at Yongbyon by the year's end (this, the main source of the North's bomb-grade plutonium, has been shut since July). North Korea has also promised to give a full account of all its nuclear activities by then. If it sticks to this pledge—and American-led inspection teams are to oversee the disablement, starting, said negotiators, as early as this month—then the North will get about $100m in aid. Meanwhile, America says it will drop the North from its list of states that sponsor terrorism, a central North Korean demand.

In Washington, DC, the administration hailed the pact, which had George Bush's personal nod, as a real step on the path to a nuclear-free Korean peninsula. Others remain sceptical until the fine print is known. And no one doubts that the next stage after declaration and disablement—getting North Korea to give up its handful of nuclear weapons along with its stock of fissile material—will prove by far the hardest. For now, Mr Kim is being given the benefit of the doubt. Not for the first time, he may turn a profit from that. Perhaps the brutalised country he has done so much to impoverish might even benefit too.

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Iraq

I want to kill you, but not today

Oct 4th 2007 | MOSUL AND QAEM
From The Economist print edition

AFP

Will American co-operation with former insurgents last?

“QAEM has no room for terrorists,” read the billboards on the desert road to this remote town in Iraq's far north-west, near the Syrian border. In a dusty grid of houses beside a strip of farmland along the Euphrates valley, parents escort their children to school and people go shopping under the watchful eyes of American troops and Iraqi police. Peace, for the moment, prevails. It was very different two years ago. The Americans hail it as a fine example of progress at last.

Qaem was one of the first areas in Iraq to be overrun by a network proclaiming an allegiance to al-Qaeda—and one of the first to throw it out. Starting in 2005, militias run by the powerful Albu Mahal tribe teamed up with the Americans in a series of offensives that has turned a former al-Qaeda stronghold into one of the safer Sunni Arab areas in Iraq. Such “tribal awakenings” are now at the heart of American strategy. The idea is to isolate al-Qaeda and similar groups by building local alliances from the bottom up, rather than wait for the politicians in Baghdad to work out a national reconciliation plan.

But the Shia rulers in Baghdad feel threatened. As the model spreads across Iraq, they fear that creating new militias in a country already swamped with them is a recipe for civil war. This week they denounced the policy for “authorising groups to conduct security outside the government's knowledge and jurisdiction” and for “embracing terrorist elements”.

In the past few months, the movement has spread from its cradle in Anbar province, west of Baghdad, to other Sunni parts of the country. In the farm belt south of Baghdad, the Americans have enlisted 14,000 “concerned citizens” into “neighbourhood watch” programmes to spot infiltration by extremists. In Diyala province, north-east of Baghdad, some members of one of the biggest Sunni insurgent groups, the 1920 Revolution Brigades, now accompany the Americans as guides on patrols and point out al-Qaeda safe houses.

In some cases the Americans have sponsored alliances against al-Qaeda, providing ammunition and security co-ordination, and arranging contracts for tribal leaders to put their men on the payroll. Al-Qaeda has fought back, notably by assassinating a leading Sunni sheikh, Abd al-Sattar Abu Risha, who led the movement from Anbar's capital, Ramadi. But that has not badly disrupted the process.

The “awakenings” probably account for the sharp drop in violence in Anbar, where nine Americans died last month, against 26 in September last year. They may also have reduced violence nationwide, measured by American and independent monitors. The civilian death toll last month was half what it was

in August.

Most Iraqi Sunni Arabs still hate the foreign occupier but many seem to have decided that al-Qaeda is a greater evil. They particularly dislike al-Qaeda's penchant for setting off huge car-bombs in populated areas; the assassinations of Iraqis who join the police or rival insurgent groups; and the imposition of a puritan version of Muslim law that sometimes, according to some reports, involves chopping off the two fingers with which smokers held their cigarettes. Some also criticise al-Qaeda attacks on Shia civilian targets, especially because they have provoked deadly reprisals by Shia militias.

But tribal leaders' motives have also been questioned. In Qaem, some claim the Albu Mahal turned against al-Qaeda partly because it had helped a weaker tribe tip the balance of power in the area. Others say that Abu Risha was a devious former highway robber who simply found a new source of income by teaming up with the Americans. In many areas where a tribal awakening is proclaimed, rows have erupted over who is a clan's true representative and who a “fake sheikh”.

More ominously, the Americans are accused of organising forces which may later turn their guns against the Iraqi government. Several Shia leaders worry that the Americans are too naive to distinguish between sincere foes of al-Qaeda and others who have co-operated with it in the past and may do so again. And al-Qaeda may have infiltrated some of the new outfits. It is rumoured, for instance, that Abu Risha was betrayed by one of his bodyguards.

In northern Iraq's Nineveh province around Mosul, Kurdish leaders are particularly worried by reports that the Americans may arm the Shammar, a Sunni tribe that controls a remote stretch of the border with Syria. Some American troops have misgivings, too, about arming people who may have killed their comrades. An American soldier's blog records a telling conversation with a 1920 Revolution fighter. “Do you want to kill me?” asked the soldier. “Yes,” replied the former insurgent, without emotion. “But not today.”

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Iran

Parallel purposes

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UN or no, the squeeze on Iran tightens

IRAN carries on enriching uranium regardless at its nuclear plant at Natanz. Diplomats from the five veto-wielding members of the UN Security Council (America, Britain, France, Russia and China) plus Germany, unable to agree on tougher sanctions in the face of such defiance, are left sucking their pencils. Does that mean, as Iran's president, Mahmoud Ahmadinejad, insists, that Iran's nuclear case is effectively “closed”?

Iran has won a reprieve at the UN. Yet the six agreed on September 28th that it must still come clean about its nuclear past and still suspend its enrichment programme if further sanctions are to be avoided. Meanwhile deepening frustration in America and Europe at the pace of UN diplomacy could mean greater economic pressure on Iran's regime, not less.

Sanctions talks are to continue among the six. So will the efforts of Javier Solana, the European Union's foreign-policy chief, to persuade Iran to suspend its nuclear work. But Iran, for its part, talks of stepping up enrichment efforts (used in fuel for power reactors but abused in bomb-making) to “industrial scale”.

Russia and China want to delay further UN action to see whether Iran is complying with a controversial “work plan” that it signed with inspectors from the International Atomic Energy Agency, the UN's watchdog, in August. By the time the IAEA's 35-nation board meets again, on November 22nd, Iran is meant to have accounted for advanced centrifuges called P-2s (able to enrich uranium a lot faster than the P-1s operating at Natanz) and their parts bought on the black market.

After years of stonewalling, Iran's centrifuge answers will be an indication of whether it will now co-operate with inspectors, though it could stop at any point. The deal lets it dribble out answers, including about military connections to its nuclear work, over months. Boasts by Mr Ahmadinejad of research using the faster P-2s—work not reported to the IAEA—have fed concerns that Iran may have a parallel nuclear-weapon programme.

As Iran takes its time with its answers, its enrichment efforts gather pace. To give it pause, driving up the cost of its defiance, America is pressing banks and businesses in Europe, Japan and around the world to cut ties with the country. A lot of European banks have cut off dollar dealings with Iran and are winding down other business; Japanese banks have been refusing new business. European exports to Iran are falling, as are government trade credits.

France's president, Nicolas Sarkozy, wants to beef up this “arsenal of sanctions” on Iran. He has called publicly on French companies not to tender for new Iranian contracts. When EU foreign ministers next meet, on October 15th, France and Britain will press the others to use the legal right they gave themselves earlier this year to extend Iran sanctions beyond those listed by the UN. Some, notably Italy and Germany, will be nervous at making trade restrictions legally binding without UN backing, for fear that competitors, notably Chinese and Russian companies, will muscle in on their hitherto lucrative patch.

Yet businesses are taking the hint. And such parallel sanctions bite more quickly than those negotiated tortuously among the six. Nor has the UN track reached its end. Despite a thirst for Iran's gas and oil, China backed earlier sanctions. Russia's president, Vladimir Putin, is expected to pay a visit to Tehran later this month. Yet he won't ship enriched-uranium fuel to Iran's all-but completed nuclear reactor while its enrichment work goes on. Iran hasn't wriggled free yet.

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The Palestinian territories

Boost here, squeeze there

Oct 4th 2007 | HEBRON, JENIN AND NABLUS
From The Economist print edition

We query a plan to rehabilitate Fatah and isolate Hamas

THEY came for Omar Maswadeh at half-past midnight. They broke furniture at his home in the West Bank town of Hebron, blindfolded him, shoved him in a car. They kept him in solitary, hooded and with his hands tied, in the painful seated *shabah* position that Israeli courts have outlawed. Two days later they came for his brother Alaa and his cousin Yusri. After holding the young men for two to three weeks each, they charged them with membership in Hamas's "executive force", a militia that the Islamist party created in Gaza but never actually managed to form in the West Bank. Then they let them go.

But the captors were Palestinian, not Israeli. The Palestinian Authority (PA) has been locking up suspected Hamas members and sympathisers all over the West Bank since June, when Hamas routed the secular Fatah's forces in Gaza after months of factional strife. Yusri Maswadeh says he was suspended by his wrists, tied behind him, from window bars for hours—"worse than with the Israelis". Fayyad Aghbar, a former head of the Awqaf (the Muslim authorities) in Nablus, the West Bank's biggest town, was not tortured but describes a fellow prisoner who was forced to kneel with his hands tied and was hit if he sat back on his haunches. Again, it was "worse than the Israelis".

AP

The Fatah faithful in Jenin

The stories everywhere are similar: arrests, beatings, intimidation—plus a concerted repression of Islamist activity. Civil servants appointed during the 15 months when Hamas ruled alone or jointly with Fatah have been demoted or fired. Many charities linked to Islamists have been shut down for "administrative irregularities". Mosques have been raided, high-school graduation ceremonies in mosques banned, Hamas materials confiscated.

PA officials—while not admitting to the torture allegations—say that the crackdown is aimed at preventing another Gaza-style conflagration. Moreover, they say, Hamas is not being targeted exclusively. A lot of the fired civil servants were appointed in a frenzy of Fatah nepotism just before Hamas came to power. Nearly 700 new charities were registered during Hamas's rule, says Sumud Damiri, the interior ministry's legal adviser, and some are clearly dubious.

The PA's policy, led by the president, Fatah's Mahmoud Abbas, and Salam Fayyad, the prime minister whom he put in charge of an interim government after firing the Hamas-led one, is two-pronged: to drive Hamas, which still rejects full-fledged peace with Israel, underground, while cleaning up some of the mess created under previous Fatah misrule. It is part of an American-led plan to boost Mr Abbas and Fatah by bettering life in the West Bank, while confining Hamas to Gaza and keeping Gaza's crossings closed to most trade (see article).

That strategy looks dubious. One reason is that the current repression of Hamas in the West Bank looks like a repetition of the Fatah-Israel collaboration in the mid-1990s, when Hamas was trying to disrupt the Oslo peace accords between Israel and the late Yasser Arafat's Fatah. Then, the PA's “preventive security” forces developed a reputation as ruthless jailers and torturers of Islamists. It rebounded on them. A decade later Palestinians—many because they were fed up with Fatah's corruption and ineptitude—voted Hamas into power. And the Fatah-Hamas blood feud exploded in June in Gaza—to Fatah's loss.

Even if Mr Abbas and Mr Fayyad manage to clean up Fatah this time, they may be bottling up radical Islamist anger that could burst out in the future. What is more, though Hamas is going underground politically and many charities are being closed, others continue to raise *zakat*, the Muslim tithe, for the social projects that built support for Hamas during its previous years in the wilderness. And though Hamas is indeed losing popularity in Gaza, thanks partly to its own heavy-handedness against Fatah, nobody has yet thought up a plausible method for removing it from power.

The other problem is that isolating Gaza undermines the policy of improving life in the West Bank. Many West Bank businesses enjoyed a healthy trade with the strip's 1.4m people. Fahim Zubeidi, head of quality control for Birzeit Pharmaceuticals near Ramallah, the capital, says the clampdown on Gaza has halved his company's sales there.

Even before that, sending goods to Gaza was hard. Delays at checkpoints in and out of the West Bank meant a lorry could take four days to complete a trip that would otherwise take no more than two hours each way. Sending a container there now costs 20,000 shekels ($5,000), as against $800 for transporting one to China, says a Hebron businessman.

Such obstacles litter the West Bank, too. Since the outbreak of the second Palestinian *intifada* (uprising) in 2000, Israel has built permanent checkpoints around most of the main Palestinian cities to protect the

Israeli settlements nestled around them. The 45-minute journey from Ramallah to Nablus now takes Birzeit's supply trucks four or five hours. From Jenin, the West Bank's northern and most isolated district, 20,000 people may have emigrated south because it is so difficult to move around.

Israel says it plans to remove some of the nearly 600 checkpoints and roadblocks in the West Bank to help make life easier. But making a serious difference would mean getting rid of the big, fixed terminals through which West Bank travellers must pass and which break the territory into a patchwork of small, near-separate economic zones—and they, because of Israel's security, will be the last to go.

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The Gaza Strip

Fatah has begun to fight back

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A new struggle for power is under way

FIRST there was one, then several, and now the yellow flags of Fatah dominate the Gaza Strip's skyline. From north to south, the bright tall banners of the secular Palestinian party easily outnumber the faded green flags of Hamas, the Islamist movement that bloodily ousted Fatah from power in Gaza in June. But Fatah has a long way to go. Its battle with Hamas is being fought out in demonstrations, by bombs and bullets, and over cash and concessions from Israel. No one has yet won.

At Fatah's headquarters in Gaza City, run by a skeleton staff in the summer after Hamas's victory, a sense of purpose has returned. Western diplomats come in a steady stream to be updated on the situation, taking advantage of Gaza's relative security since Hamas took control, even though their governments do not let them speak to the movement's representatives.

Ahmed Hallis, a Fatah leader in Gaza, points to the flurry of yellow flags and tells the diplomats that Fatah is resurgent and preparing to take back power, letting only unimpeachable characters return to its ranks. Yes, the party was tainted by corruption; its domination by Muhammad Dahlan, who was close to Fatah's overall leader in the West Bank, Mahmoud Abbas, was a mistake. “The flags you see everywhere mean that Fatah is the spine of the Palestinian revolution,” he says. “Fatah must renew itself and take over again.”

Hamas's politicians say they accept a strong Fatah presence in Gaza but their security forces plainly do not tolerate dissent. Many Gazans complain that Hamas's thuggish police, known as the executive security force, arrest and beat up anyone suspected of Fatah sympathies. As a result, Fatah has been organising street protests and has boycotted mosques on Fridays.

Some 20 roadside bombs have apparently been set off against Hamas forces since they took over the strip, albeit with no loss of life. This week three former members of the naval police that Fatah used to run were killed when a bomb went off in their car. Hamas said it would have been used against the Islamists; such incidents are used to justify the arrests and torture of Fatah people. Raji Sourani, who runs the Palestinian Centre for Human Rights in Gaza, gets daily reports of arbitrary arrests and beatings by Hamas forces.

Money plays a big part in the battle for hearts and minds. Hamas says it will be able to pay 14,000 monthly salaries, averaging $400, to its staff on October 10th; the Fatah-run Palestinian Authority (PA) in Ramallah will pay around 60,000 Gazan employees—as long as they stay at home and do not work for Hamas. The PA and Hamas are both offering gifts of $100 to poor families over the Eid, the festival that starts this year on October 13th to mark the end of the fasting month of Ramadan.

Crowds of men consult lists pasted on walls in Gaza City's main street, then queue at banks to get their cash. Hamas says it is giving $100 wads to 40,000 families, while the PA is helping 65,000. It is unclear how much they overlap.

Meanwhile, Israel's near-ban on trade in and out of Gaza has made illegal business flourish. Cigarettes have more than doubled in price, prompting a new spurt in digging tunnels under the border with Egypt, which also funnel weapons and explosives. So some are doing well out of the sanctions. But those with no ties to Hamas, Fatah or the criminal gangs have little to look forward to this Eid.

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Somalia

Breaking into even smaller bits?

Oct 4th 2007 | NAIROBI
From The Economist print edition

Even the parts of Somalia that were steady are looking shaky again

Get article background

A PECULIARITY of Somalia is that while the south of the country, including its broken capital, Mogadishu, has burned, the north has been stable. Now, to the horror of those trying to put Mogadishu back together again, the north is beginning to crack too. Fighting broke out this week between Somaliland, the northern strip that has been virtually independent of the rest of the country for some 16 years, and Puntland, a semi-autonomous territory in the north-east (see map). Somaliland says it has driven Puntland forces out of Los Anod, a town in the disputed Sool region, killing six Puntlanders and injuring or capturing another 40-plus. Puntland says its soldiers have retaken the town. Yet another war seems to be breaking out.

Sool is split between sub-clans backing either Somaliland or Puntland, while some of them want autonomy for Sool itself. Somaliland, a former British colony that was separate from the larger parts that were run by Italy, declared independence in 1991 and has since sought international recognition. Puntland's sense of identity is less strong; it has seen itself as a building block for a future federal Somalia.

But Puntland is losing its grip. The Sool dispute has been compounded by the secession of much of the Sanaag region from Puntland, to form yet another self-governing entity in the north. Drawing on its history as a sultanate, Sanaag declared independence in July, renamed itself Makhir, and chose Badhan as its capital. Tension between Makhir and Puntland is high.

A still worse headache for Puntland is the departure of its strongman, Abdullahi Yusuf, to become president of Somalia. He ran Puntland with authority and ambition, grandiosely hoping to turn it into the Horn of Africa's Dubai. When he went south, he took with him a lot of Puntland troops, vehicles, weapons and ammunition. Their departure emboldened other northerners with dreams of secession or autonomy, and may give Somaliland the edge if the dispute over Sool leads to war.

Oil and gas add fuel to the ferment. Exploration rights in Puntland have been sold several times over. Somalia's prickly prime minister, Ali Mohamed Gedi, was furious when Mr Yusuf signed oil agreements without telling him, including one with a Chinese company. Mr Gedi has also refused to endorse exploration deals signed by Puntland's government.

Meanwhile, Mogadishu is getting worse again. Fewer children are going to school. The city's markets are stagnant—quite the opposite of the government's assertions that things are back to normal. Government troops and the Ethiopian forces propping up Somalia's government are still being attacked by bombs, grenades and snipers of the Islamist militias ousted by Ethiopians early this year. The African Union promised to send 8,000 peacekeepers and then hand authority to a UN mission later this year. But several AU countries failed to honour their pledges. Uganda is still the only African one to have sent troops; with just 1,600 of them there, the UN is unlikely to come in and take over.

The American administration and other Western governments still want to back Somalia's transitional government until elections due in 2009. A recent reconciliation conference in Mogadishu passed off without rancour, itself something of a success, and was bolstered by the apparent failure of a rival meeting, mainly of Somali Islamists, in the Eritrean capital, Asmara.

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South Africa

A Scorpion is stung

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Why has the country's national prosecutor been suspended?

Get article background

AS THE business of nominating candidates for the leadership of the ruling African National Congress (ANC) gets under way this week, the atmosphere, already clouded by arguments over who should succeed President Thabo Mbeki as party leader, is turning nastier. Mr Mbeki recently suspended Vusi Pikoli, head of the National Prosecuting Authority (NPA), who oversees an investigative unit known as the Scorpions, for an “irretrievable breakdown” in relations with his boss, the justice minister.

It has since been reported that, before his suspension, Mr Pikoli had taken out a warrant to arrest Jackie Selebi, who heads the South African police. An inquiry has now been launched into whether Mr Pikoli—but not Mr Selebi—should be fired. But the government has been so vague and tight-lipped about Mr Pikoli's suspension that it is feeding a host of conspiracy theories that could affect the ANC's selection, in December, of the party's next president. Whoever wins that contest is virtually certain to become the country's next leader too.

Mr Pikoli has overseen the most recent bout of the NPA's six-year investigation into the activities of Jacob Zuma, the country's former deputy president, who was fired in 2005 but still seeks South Africa's top job. Charges of corruption and fraud against Mr Zuma were dismissed last year. But the NPA has not ruled out the possibility of charging him again.

The Scorpions, set up in the late 1990s to investigate corruption and organised crime, have been accused of abusing their power and being used to settle political scores. Critics say they should be disbanded or absorbed into the police. A government-appointed commission suggested they be kept within the NPA but report to the minister of safety and security.

Mr Selebi has been under fire for some time for the country's breathtaking level of violent crime. Calls for his sacking became more strident when he admitted to being a friend of Glen Agliotti, a suspected crime boss arrested by the Scorpions. They have been investigating Mr Selebi, who insists his hands are clean and has kept his job.

The opposition has been demanding a fuller explanation, so far in vain. Mr Pikoli secured impressive conviction rates. But did he overstep his authority? He is said to have kept his boss in the dark over several big cases, including Mr Selebi's. And people disagree over what the NPA's independence really means. The opposition has questioned the independence of the inquiry into whether Mr Pikoli is fit for the job, since it is being headed by an ANC veteran and former speaker of parliament, Frene Ginwala.

Was Mr Pikoli's suspension due to the arrest warrant? People in the president's office deny that the decision was meant to protect Mr Selebi and refuse to say whether a warrant for his arrest was ever obtained. So does the NPA. But Mr Mbeki's reluctance to explain things more fully has fuelled suspicions that state institutions are subject to the vagaries and bitter rivalries of ANC politics.

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Vladimir Putin

The never-ending presidency

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Illustration by Peter Schrank

The president unveils his plan for staying in power after next March

IT HAS always been a question of how, not if, Vladimir Putin would retain power in Russia when his second, and (according to the constitution) final presidential term runs out in March 2008. This week Mr Putin lifted the veil. At a congress of the pro-Kremlin United Russia party, he graciously agreed to head its party list at the general election in December. He added that he may become prime minister if the party wins the election and the president is a man he can work with. United Russia is sure to win and, since Mr Putin will hand-pick the president, he will presumably get along with him. So this charade has only one meaning: Mr Putin is staying on, probably for a very long time.

This is part two of Mr Putin's game plan. Part one came three weeks ago when he appointed an unknown technocrat, Viktor Zubkov, as prime minister and hinted that he might become president. Mr Zubkov has three main qualifications: he has no visible political ambitions, is quite old (66, to Mr Putin's 54) and is personally loyal (he was Mr Putin's deputy in St Petersburg's mayoral office.)

Now Mr Putin has a couple of options. He could take a short break from the Kremlin and move into the prime minister's chair, leaving Mr Zubkov (or another pliant candidate) to look after the Kremlin for a while. Mr Zubkov would then step down, perhaps for health reasons, and Mr Putin would automatically return as president without breaking the letter of the constitution. His other, more complicated option, is to use United Russia's dominance of the Duma, the lower house of parliament, to change the constitution and devolve real power to the prime minister, turning the presidency into more of a ceremonial job. This would also allow him to stay in power without the appearance of breaking the constitution.

Either plan has risks. His popularity may not transfer easily to somebody like Mr Zubkov, who uncannily resembles the Soviet-era collective-farm director that he once was. Any more colourful candidate could renege on a deal. The idea of two power-centres in Russia, even for a short time, poses problems, particularly when rivalry between factions in the Kremlin is intensifying.

In the short term foreign investors are taking comfort from Mr Putin's move. Western leaders may hold their noses, but they will continue to deal with Mr Putin much as they do now. In the longer term, Mr Putin's plan does not bode well for the economy or for political stability. More important, it will do nothing to make it easier to solve any of the country's huge problems, such as the state of the army, rampant corruption, a health-care crisis or a looming demographic crunch.

In the words of Lilia Shevtsova, a political analyst at the Carnegie Moscow Centre, the plan “eliminates politics” and closes down the channels of social mobility for many aspiring Russians. By staying in power after 2008, Mr Putin may have made himself, in effect, a Kremlin hostage; he has also overridden one of

the big achievements of the Yeltsin era: a voluntary transfer of power from one political leader to another.

Kremlin ideologues like to describe Russia as a “sovereign democracy”, whatever that means. Elsewhere it would be called an autocracy. It has nothing in common with a real democracy, which implies competition for power. Mr Putin likes to talk about his country's revival and greatness. Yet, for all his talk, he treats his people with contempt, reducing the political process to a Byzantine and meaningless guessing-game. “Isn't it fun? The president appears in public, stretches out two closed hands and asks cunningly: where is the sweet? That is the only question deemed suitable for the population,” Lev Rubinshtein, a Russian essayist, wrote this week.

Disconcertingly for critics, the vast majority of the Russian population seems to like the game and to support Mr Putin, whose popularity rating is consistently above 70%. The lack of independent television is only one reason for this. The bigger point is that Mr Putin's rule has coincided with a spectacular rise in oil prices, leading to improved living standards for millions of Russians. As one United Russia delegate who pleaded with Mr Putin to stay in power put it this week: “Vladimir Vladimirovich, you are lucky! And while you are the president, luck follows Russia. For tens of millions of people you are a token, a symbol of Russia's successful development.” Yet luck, like oil money, tends to run out sooner or later.

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Ukraine's election

Oranges and lemons

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Yulia Tymoshenko wins, but there are still doubts surrounding her coalition

TWO hours after the polls closed in Ukraine's election on September 30th the opposition leader, Yulia Tymoshenko, strode into a private suite in Kiev's smartest hotel, where European observers were waiting. At that moment Viktor Yanukovich, the incumbent prime minister, appeared on television looking shell-shocked. The exit polls were still coming in, but the first results were reflected on the politicians' faces. “We have the right to form the new government,” Mr Yanukovich bleated. “Oh dear,” said Ms Tymoshenko, before switching off the television, “he does look like an upset child.”

Days later Mr Yanukovich had bounced back. His Party of the Regions took the biggest share of the vote, as it had in March 2006. But the momentum is still running Ms Tymoshenko's way. She is the only politician whose popularity has risen sharply, boosting her party's share of the vote from 22% 18 months ago to almost 31%. With Our Ukraine, the party of President Viktor Yushchenko, taking 14%, there is a tiny majority for an “orange” coalition with Ms Tymoshenko as the most likely prime minister.

Forming that government depends on Ms Tymoshenko and Mr Yushchenko sticking together. On October 3rd Mr Yushchenko called on all three parties to start talks over a coalition. But Ms Tymoshenko promptly said she could not work with Mr Yanukovich, as did some members of Our Ukraine.

The voters' strong support for Ms Tymoshenko suggests that, for all their disillusionment in the past few years, they want reform just as much as they did when they poured into Kiev's Independence Square in the snows of late 2004. The orange revolution that pushed Mr Yushchenko into the presidency instead of Mr Yanukovich turned Ukraine from a corrupt post-Soviet autocracy into a fragile democracy. That Mr Yushchenko's support is now relatively weak reflects not a change of mood but his failure to live up to the orange revolution's promises.

The latest election has restored the divide between the Party of the Regions and the orange coalition. This same line separates a post-Soviet thuggish political culture from a proto-European one. If Mr Yushchenko tries to blur the line by working with Mr Yanukovich, as he did in 2006, he is likely to land the country in a new political crisis.

For all the faults that became evident when she was briefly prime minister in 2005, Ms Tymoshenko has remained consistent. Unlike Mr Yushchenko, she has always rejected the idea of forming a coalition with her opponents. Unlike Mr Yanukovich, she has not tried to change her image with the help of American spin-doctors. In the eyes of millions of Ukrainians, she is still the blonde heroine of the orange revolution and a victim of, not a participant in, the infighting among the president's men.

She promises a break with the past that appeals to those who feel let down by successive governments. And she has broad support. Mr Yushchenko draws his vote largely from the west of Ukraine, and Mr Yanukovich from the Russian-speaking east and south. Ms Tymoshenko is less territorial: most of her voters live in central Ukraine, but in this election she has made inroads in both east and west. The risk of Ukraine splitting down the River Dnieper was always overdone. After this election it looks smaller still.

Ms Tymoshenko avoids the sensitive issue of making Russian a second official language and no longer pushes for early entry into NATO, opposed by the south and east. Like most of her countrymen, she believes that the future of Ukraine lies in the European Union. But, claims Hryhory Nemyria, her chief adviser, there is a distinction. She does not see membership as a reward to be handed out merely for breaking out of the post-Soviet space, or as a source of quick economic goodies. “To her, being part of Europe means modernising Ukraine first,” he says. “We can only come as close to the EU as we are ready.”

She also promises to clean up chronic corruption and sever the links between business and politics. (Each party in Ukraine is backed by powerful business interests, including her own.) Having made her fortune in

murky gas trades between Russia and Ukraine in the early 1990s, Ms Tymoshenko now says she will eliminate all shady intermediaries and make the gas trade transparent. As soon as she emerged as a potential winner this week, Gazprom, Russia's gas giant, started growling about the $1.3 billion of debt Ukraine owes for gas and threatened to cut off supplies, just as it did in January 2006.

Ms Tymoshenko is the most professional politician in Ukraine, but also the most populist. She has promised within two years to reimburse the savings people lost when the Soviet Union collapsed—a pledge even her advisers say is unrealistic. Her period as prime minister in 2005 was marked by talk of reviewing privatisation deals and capping fuel prices. But she has learnt lessons, says Mr Nemyria, and is now more pragmatic. Whatever she does, though, she will be held accountable by those who voted for her, because Ukraine has since 2004 become a recognisable democracy in which power is granted and taken away on the basis of elections that are broadly free and fair.

That is the biggest achievement of all by this former Soviet republic, and it is appreciated by losers as well as winners. As Yuri Miroshnychenko, a young member of the Party of the Regions, puts it: “There is no absolute power in Ukraine. We can work in opposition and her coming to power is not a tragedy for us. The most important thing is that Ukraine is moving in the right direction. Today it is becoming Europe. There is no way back.”

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Georgian politics

Saakashvili's test

Oct 4th 2007 | TBILISI
From The Economist print edition

A worm in the bud of the rose revolution?

AS BEFITS a land of film-makers and actors, Georgia likes to play its politics as spectacle. That is why, on September 28th, Rustaveli Avenue, in Tbilisi, was again awash with demonstrators. Echoes of the rose revolution of four years ago are faint: the numbers were far smaller and most of the protesters older. But by bringing the crowds on to the same streets as in November 2003, the opposition made a telling point against President Mikhail Saakashvili.

The man whose arrest on corruption charges drew out the protesters is a former defence minister, Irakly Okruashvili. At 33, he is younger and more hotheaded even than Mr Saakashvili. He once promised to celebrate new year in Tskhinvali, capital of the breakaway territory of South Ossetia. Mr Saakashvili sacked him last year. Mr Okruashvili brooded silently for months before producing lurid allegations against his former boss. He has accused the president of ordering the murder of a Georgian media magnate, Badri Patarkatsishvili, and has cast doubt on the death in 2005 of the then prime minister, Zurab Zhvania, officially in an accident.

Yet it is Mr Okruashvili's charges of corruption in the president's inner circle that may be more damaging. Mr Saakashvili made his name as a crusader for honest government and against nepotism. Mr Okruashvili now looks like the jilted outcast of a clan that bends the law in its own interests. He has put before Georgians some ugly questions that need answering. Mr Saakashvili has dismissed Mr Okruashvili's claims as “unpardonable lies”—but he has not answered them directly.

On the whole, Mr Saakashvili's young team has transformed Georgia for the better, increasing tax revenues and overhauling the public sector. But critics say some measures have paid scant regard to due process. Allegedly corrupt officials have been arrested on television and made to pay fines directly into the state budget. Prisoners have been ill-treated. Shopkeepers and residents of Tbilisi complain that their property rights have been flouted in the name of rebuilding the city. The leaders of a bloodless revolution in a poor country now preside over one of the world's fastest-growing defence budgets.

A host of discontents has crystallised around the arrest of Mr Okruashvili. Eight opposition groups have united into one. Mr Saakashvili is losing the aura he once had of being the sole undisputed leader of Georgia. In the past he has faced down critics with histrionics and theatrical brinkmanship. A sober response, not so far in his political repertoire, may now be called for.

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French mayors

Suburban style

Oct 4th 2007 | PARIS
From The Economist print edition

Nicolas Sarkozy picks one of his own to take his old job as mayor of Neuilly

Get article background

TO BE mayor of Neuilly-sur-Seine is to be in charge of a suburb that is a cross between Notting Hill in London and New York's upper east side. This swanky place west of Paris is home to a constellation of French film stars, media barons, business chiefs and politicians. They meet each other at weddings or the school gates as often as they do in the boardroom or television studio. Neuilly's most famous ex-mayor happens to be running the country: Nicolas Sarkozy. He even met his future wife, Cécilia, when, as mayor, he conducted her civil marriage to her first husband.

So it was with unusual interest that the French found out the identity of the candidate for Neuilly from Mr Sarkozy's UMP party at next March's municipal elections: David Martinon, the president's spokesman. On September 30th Mr Sarkozy showed his support for his 36-year-old protégé by accompanying him to Neuilly town hall, which he had first won in 1983 at the age of 28.

Needless to say, the parachuting-in of Mr Martinon has ruffled feathers. There was no primary to make the choice, though Mr Sarkozy insisted on one for the UMP candidate for Paris. Some party members even heckled Mr Martinon. Their favourite, Arnaud Teullé, is, unlike Mr Martinon, locally elected and deputy to the present mayor. He has now had to accept second place on the electoral list.

Dominique de Villepin, a former prime minister and rival of Mr Sarkozy's, also wondered if being mayor of Neuilly was “compatible” with being the president's spokesman. Mr Sarkozy is unworried by France's tradition of double mandates—he is letting ministers stand for mayorships next March. Yet knowing that the mayor is not only the mouth of the president, but also has his ear, is likely to prompt some intense lobbying by constituents in Neuilly.

If Mr Martinon transforms himself into a fully fledged politician, it will be largely thanks to lessons he has learnt from Mr Sarkozy. Even before last spring's presidential election, Mr Martinon accompanied his mentor everywhere, discreetly sitting in on top-level meetings with heads of state and government. Now, his hair and his suits more classically cut, he has become a public face, conducting weekly White House-style briefings in an effort to freshen up crusty presidential communication. Mr Martinon was a natural choice as spokesman, since he can claim to know Mr Sarkozy's views as well as anyone else. Whether he will also be able to claim to know those of the good burghers of celebrity-studded Neuilly is another matter.

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Italy's budget

Too much

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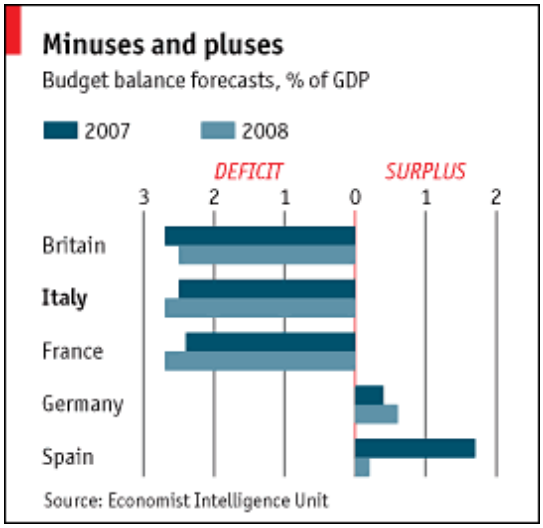
The 2008 budget gives companies a break but leaves spending too high

IN ITALY, Romano Prodi once mused, it can be hard "to distinguish the real issue—about which nobody ever talks—from the fictitious one which is fought over ferociously." Rarely has that been truer than of the debate over the draft 2008 budget presented by Mr Prodi's centre-left government. Ironically the person responsible for the confusion is Mr Prodi himself.



On September 29th he emerged from an 11-hour cabinet meeting to announce that the low-paid would get reduced property taxes and either an income-tax break or a cash handout. But he scarcely mentioned the most significant measure: a cut in the corporate-tax rate from 33% to 27.5%. The budget also trims a regional business tax. Together, these may boost the economy without unleashing inflation, which might flow from income-tax cuts of the sort being urged by the opposition.

For public consumption, it is being said that this apparent giveaway to industry will not cost a cent, because the budget also widens the corporate-tax base by scrapping many tax breaks. But officials privately admit that this is nonsense. The corporate-tax rate is to fall by a sixth, which will soak up much of the extra €18 billion ($25 billion) that Mr Prodi's finance minister, Tommaso Padoa-Schioppa, has raked in by squeezing tax evaders.

The reason nobody admits this is to avoid upsetting Italy's trade unions and their allies in government, who could bring down Mr Prodi's shaky coalition. The left has already forced him to water down pension reforms. The unions have secured a modest €700m package of welfare reforms that they are now putting to a vote of their members. A rejection would be disastrous. So this is not a good moment to be highlighting what many Italians might see as a bosses' bonanza.

Mr Padoa-Schioppa claims that his budget will reduce the deficit from 2.4% of GDP this year to just 2.2% in 2008, less than in Britain and France. He also expects the public debt to shrink from 105% to 103.5% of GDP. This is not enough for the rating agencies, which have grumbled that he ought to do more to repair Italy's public finances. But Mr Padoa-Schioppa has reversed a trend of rising deficits and debt only by inflicting real pain—not only by improving tax collection but also by raising tax rates. The government had to give a sign to payroll employees, who cannot dodge because their tax is deducted at source, that there are benefits from the clampdown on the less honest of their self-employed peers.

A more pertinent criticism of the 2008 budget is that it again shrinks from spending cuts. The public sector takes over half of Italy's GDP, and it spends it badly. Waste, corruption, overstaffing and underperformance make for a huge burden on the economy. It is an issue about which Mr Padoa-Schioppa cares passionately. Last month, his department sent a "green book" to ministers detailing where they could make cuts. But that would pit them against trade unions and other vested interests. It is perhaps too much to ask of politicians with a single-vote majority in the upper house of parliament.

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Turkey and Armenia

Genocidal follies

Oct 4th 2007 | ISTANBUL AND YEREVAN
From The Economist print edition

The trouble that might flow from an American congressional resolution

A RECENT evening in Istanbul, Turkey's (and Europe's) biggest city. Armenia's leading musician, Djivan Gasparyan, is playing his *duduk*, an Anatolian-style clarinet, as Yavuz Bingol, an ethnic Kurd, belts out Turkish folksongs. The event symbolises a budding rapprochement between ordinary Turks and Armenians. But America's Congress may now torpedo this fragile process by voting for a bill calling the mass slaughter of up to 1m Ottoman Armenians in 1915 a genocide.

Turkey has squashed previous attempts to pass such a bill by exploiting its strategic significance and its clout as NATO's only Muslim member. This time officials fret that not only will a congressional committee approve the resolution but also it may pass on the House floor. Turkey says that this would plunge relations with America into deep crisis. “Placing the Turks in the same category as Nazis is intolerable for us,” says one official.

Possible retaliatory measures might include denying the Americans the use of the Incirlik airbase in southern Turkey, which is a hub for the supply of non-combat materiel for American troops in Iraq and Afghanistan. Turkey could also seal its land border with Iraq. With positive Turkish views of America at a low of only 11%, according to a recent German Marshall Fund poll, such moves might give nationalists in Turkey a big boost.

Nancy Pelosi, the House speaker, whose Californian district includes many rich Armenians, is unswayed by pleas to back down. Eight former secretaries of state have written to her to argue that, besides endangering “our national security interests”, the bill would kill “some hopeful signs already that both parties are engaging each other”. Vartan Oskanian, Armenia's foreign minister, retorts that “expressing concern about a process that doesn't exist is disingenuous”. His own recent meeting with his Turkish counterpart, Ali Babacan, in New York got nowhere.

Turkey has no diplomatic ties with Armenia and refuses to open its border with the landlocked ex-Soviet republic. This was sealed in 1993 after Armenia occupied a chunk of Azerbaijan in a vicious little war. Air links have been restored, however, and recently Turkish diplomats have hinted at a more dramatic move: formalising ties, over the objections of a vocal Azeri lobby in Turkey, not to mention those of its hawkish generals. In exchange Armenia would have to recognise its border with Turkey and make some conciliatory gesture towards Azerbaijan.

Armenia counters that it wants to restore relations “without preconditions”. That is because of a widespread suspicion that Turkey is feigning change merely to derail the genocide resolution. If Turkey were sincere, say the Armenians, it would scrap article 301 of the penal code, under which intellectuals have been prosecuted for daring to call the Armenian tragedy a genocide. On October 3rd Turkey's new president, Abdullah Gul, duly called for changes to article 301 in a speech to the Council of Europe.

Turks claim that they want to delink the issues. As one official puts it, “we strongly believe in decoupling our ties with Armenia from the genocide bill and feel that over time the relationship will flourish on its own merits.” Should the bill be adopted in Congress, though, a change in policy would become impossible because of the nationalist passions it would stoke. These worries are shared by Turkey's Armenians, still reeling from the murder in January of an ethnic Armenian newspaper editor, Hrant Dink. Mr Dink's lawyers claim that the nationalist teenager who shot him was acting under orders from rogue elements within the security forces.

David Shahnazarian, a former chief of Armenia's National Security Council, complains that Western countries are using the genocide issue to promote their own agenda. “In the case of France, it is to keep Turkey out of the EU,” he says. The massacre of a million civilians is a matter in which Turks should arrive at the truth on their own. But as Mr Gul has partly conceded, that may necessitate an end to article 301's restrictions on free speech.

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Charlemagne

The China trade syndrome

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Illustration by Peter Schrank

Europe's next big globalisation row will be over trade with China

EUROPE'S political leaders are bracing themselves for a big new row about global competition: over China. The China threat has become well-embedded as a motif of American politics, with a stash of China-bashing bills always lurking in Congress. But Europeans have taken longer to wake up to China's rise. That is partly because fears of globalisation at first meant worrying mainly about people moving from central Europe westwards and factories moving in the other direction, suggests Katinka Barysch, at the London-based Centre for European Reform. While Americans were talking about “the China price”, she says, “we were still talking about the Polish plumber.”

This mythical figure, branded a public menace to the French people just before they voted down the draft EU constitution, appeared in 2005, during a previous anti-globalisation spat. There was a xenophobic edge to the talk of invasion by low-paid, lightly regulated workers from the EU's newest members. But the debate quickly drifted into pantomime. The Polish tourist board hired a beefy model to pose as a plumber, promising that he was staying in Poland, and inviting tourists to come and admire him. A row about China threatens to be far more serious.

A chat about globalisation at an informal summit of European leaders in Lisbon later this month will be one possible flashpoint for the new row. Another will be a planned EU-China summit in November. In the words of one official, the EU may soon be “nostalgic” for quarrels over Polish plumbers. Three linked China problems are now causing big ructions.

The first is one of sheer scale. Low-key policies that seemed adequate a couple of years ago have struggled to keep pace with the explosive growth of trade. Two-way trade between the EU and China expanded by over 20% last year to a total value of €254 billion ($319 billion), and the trade balance has swung sharply in China's favour. Compared with America, the EU has shunned confrontation, preferring dialogue with China over such concerns as the deficit or intellectual property. But this calm approach may be a harder sell when the bilateral trade deficit with China is running at an average of €15m an hour.

The second problem is that China ignores gentle hints to stick to commitments it made when it joined the World Trade Organisation. The charges are numerous: there are perennial (and hard to prove) accusations about state subsidies and a failure to guard against the theft of intellectual property. A bleak report by the EU Chamber of Commerce in China notes a fresh threat: the unequal treatment of foreign companies by newly muscular Chinese regulators. Chinese officials are even accused of diverting EU energies into “process”—endless argument over when and with whom meetings will take place. It does not help that many commissioners fall for this nonsense, tripping over each other in their eagerness to visit China and meet the right officials. The 27 member countries are worse, eagerly undermining agreed positions in a quest for national advantage.

The third problem is China's currency, the yuan, which has lost about 40% of its value against the euro

since 2000, making Chinese exports ever cheaper. President Nicolas Sarkozy of France loudly argues that euro-area governments should join forces with the European Central Bank (ECB) and back American demands for the Chinese to let their currency appreciate (it is still loosely pegged to the dollar). But the sad reality is that any finger-wagging by the Europeans might serve only to expose their impotence. Noting the euro's steady rise against the yuan, several American analysts conclude that the Chinese have taken a deliberate decision to allow Europe to foot the bill for any small concessions they may offer to America on the yuan.

Superficially, this impotence is odd. As a single trading block, the EU is by some way China's largest trading partner. Every year, more Chinese diplomats are posted to Brussels to study EU regulations (there are said to be four Chinese officials whose sole task is to monitor the European Parliament).

Divide and rule

But China knows perfectly well that the EU functions only rarely as a single block. It has learnt from experience how easy it is to divide the Europeans on tough political questions such as their arms embargo on China. Moreover, EU citizens cannot even agree on whether China is an economic threat or an opportunity. Some countries, such as Germany and Sweden, make lots of money selling machine tools and other capital goods to China. In southern Europe, businessmen complain vociferously that their traditional exports such as shoes and textiles are being killed by China. In eastern Europe, businesses built on (relatively) cheap labour fear China mightily.

Once a China row starts, camps will quickly form. Unsurprisingly, France is likely to lead calls for “negative reciprocity”: ie, slamming markets shut unless China heeds EU demands. Britain will take the opposite view, arguing for open markets as desirable in themselves. British officials are hostile to calls for action against “sovereign funds” flush with the cash of foreign governments, seeing these calls as another recipe for protectionism. Germany may be the swing voter in such cases.

Yet regardless of the economics, an argument can be made that it may become politically impossible for Brussels to seem inactive on China without further damaging fragile support for free trade. Already, complaints about Chinese goods being dumped at below production cost take up an inordinate amount of time (recent footling disputes have involved light bulbs and tinned satsumas). One response may be to go after China on non-footling disputes, but strictly within the context of enforcing rules and legally binding commitments. This could mean taking China to the WTO a lot more often. That could prove bumpy, but less so than an outbreak of xenophobic China-panic that no amount of pantomime can soothe.

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Polls and elections

One man, one decision

Oct 4th 2007
From The Economist print edition

Illustration by David Simonds

Public-opinion surveys cannot tell the prime minister when to go to the country

Gordon Brown

IT MAY not have been seriously intended at first: a chance to hog the headlines during his rivals' party conferences; a hard-to-resist game of keeping the opposition off-balance and derailing its carefully scheduled build-up to a 2009 election. But the prime minister, Gordon Brown, is discovering that low political tactics can take on a life of their own. By refusing to rule out a snap election this autumn, he has allowed speculation to run wild. Mr Brown will now find it hard to get off the tiger's back, even if his natural caution tells him to.

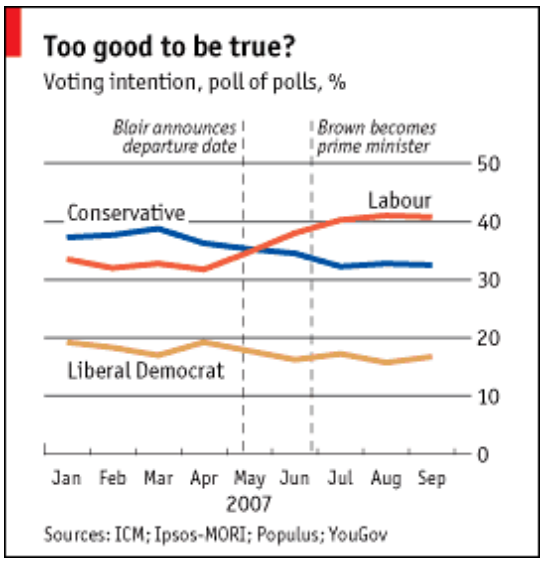
Britain gives its prime minister great latitude in timing elections. A parliament sits for up to five years, and within that span he may call an election with only 17 working days' notice. So prime ministers try to read the political and economic runes and schedule elections to their own advantage.

Mr Brown has no need to go to the country: he has a working majority of 69, a mandate that runs until the summer of 2010 and, so far, an agenda little different from the one his party won with in 2005. But readable runes abound, beginning with his meteoric rise in the opinion polls.

For most of the final, bickering year and a half of Tony Blair's premiership, the Conservatives, under their new leader, David Cameron, outstripped Labour in the polls. That changed as Mr Blair's departure drew near and the Tories began to blunder: in June Labour overtook the Tories (see chart). Since then Mr Brown has seen off terrorists, floods, sick cows and anxious bank depositors to consolidate his lead. In late September four polls put Labour an average of eight points ahead.

Mr Brown's personal approval ratings are also solid: he is more trusted than his principal opponent on the economy, health care, and even law and order. And he may have convinced voters that his predecessor alone was to blame for the unpopular war in Iraq, not least by upstaging the Conservative Party conference (see article) with a pledge to cut troop numbers there by a further 500 by the end of the year. That might account for the suggestion in some polls that women are turning away from the

boyish Mr Cameron to the craggy prime minister.



With opinion-poll ratings like these, Mr Brown's Labour would seem a shoo-in at an early election. In the last one its share of the vote was only three points higher than the Tories', but the first-past-the-post system, and the less-even distribution of Conservative voters, translated this slender preference into 356 seats in the 646-member House of Commons.

But opinion polls have not always proved a reliable guide. In eight of the ten elections since 1966, pollsters found more support for Labour than actually existed. On the eve of the 1992 election, only one poll put the Tories ahead, and then by only 0.5%; on the day, the voters made it 7.5%. No one knows if this bias has been fixed.

Then there is the matter of turnout. This may be poor if voters resent being asked to vote again so soon, and for no compelling reason; Labour voters are believed to be especially fragile. Throw in the fact that, with no election formally imminent, pollsters have been asking hypothetical questions and getting off-the-cuff answers; then a quick reminder that polls are, like all random samples, subject to statistical errors. Suddenly, those impressive polling results are less solid than they look.

Their most serious limitation, however, is that elections are lost and won in marginal seats, and the national mood is not a good guide to what happens there. This is partly because marginals are the target of most pre-election effort: party bigwigs visit, activists campaign door-to-door, posters are pasted all over town. Mostly it is because they are where tactical voting happens, and this is hard to predict.

In recent elections, supporters of Labour and the Liberal Democrats, Britain's third party, have voted for each other to keep the Tories out. If Mr Cameron has succeeded in “decontaminating” his party's brand, this coalition may break down. But most tactical voters do not decide to defect until just before an election.

Rumour has it that Mr Brown is privately polling in important marginal seats. But there is no reliable demographic data at this scale, says Peter Kellner of YouGov, a pollster, so the technical difficulties would be formidable. The cost would be too, says John Curtice, an election-watcher at Strathclyde University. A full opinion poll would need to be carried out in each constituency, with large numbers questioned to keep the margin of error low.

Mr Brown has reasons other than his surprising popularity to want to call an election now. The economy, which grew with his hand on the tiller by an average 2.8% a year between 1997 and 2006, is likely to expand by less from now on. Spending is set to tighten. And people may in time perceive that problems which Mr Brown is judged to have handled brilliantly as prime minister are in part the result of mistakes he made as chancellor.

Against such considerations, Mr Brown must weigh the appalling risk of going early. For the gamble to be worthwhile, he must do more than win; he must at least match his predecessor's tally of seats.

In 2005 the most accurate predictions came not from the opinion polls but from online betting markets. This time, says Leighton Vaughan Williams of Nottingham Trent University's Betting Research Unit, an election before Christmas is odds on and Labour is hot favourite to win the most seats. But the odds that Labour will get an overall majority are just slightly better than even. “So,” asks Mr Vaughan Williams, “is the prime minister willing to risk his majority on the toss of a coin?”

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Preparing for an election

Dust off those ballot boxes

Oct 4th 2007
From The Economist print edition

A last-minute election could leave many disenfranchised

EVEN the most carefully calibrated polls can be knocked off course by circumstances on election day. Wet and windy weather has been known to drag down voter turnout (ominously for Mr Brown, Labour supporters are said to be the most easily tempted to stay at home on cold November nights). But institutional failings can have a far larger impact. In the Scottish parliamentary elections, held on May 3rd, nearly 142,000 votes were rejected, or 3.4% of those cast. Most blamed a confusing ballot paper; a new voting system and electronic counting may have added to the muddle. An official investigation is due to report in the week beginning October 22nd—embarrassingly close to a November election, should one be called.

Britain's national parliament has stubbornly stuck with the idiot-proof first-past-the-post system, making such confusion unlikely. But calling a snap poll increases the chances of other tangles. On September 30th John Turner, the chief executive of the Association of Electoral Administrators, warned that a last-minute election would present “probably the worst [logistical challenge] in living memory”. Britain's elections now rely heavily on computers and a chain of private companies, so they need longer lead-in times than in the past, he said. Recent general elections have coincided with local ones, which are scheduled well in advance. A stand-alone general election, by contrast, could legally be called with only 17 working days' notice.

Changes to the law on postal voting worsen the administrative migraine. In 2001 postal votes were offered to all in a bid to increase turnout. Four years later, a vote-rigging operation by Labour councillors was discovered in Birmingham, so in 2006 it was decided to make applicants submit in advance their signature and date of birth, which computers were to compare with the same information on their ballot when they voted.

On the system's first outing, in local elections in May, all did not go well. Those who had changed their signature or absent-mindedly written the wrong birth date had their votes rejected. The software was so glitchy and slow that returning officers double-checked fewer ballots than before—an odd result for a system that was supposed to improve accuracy. Such teething problems can be overcome, but a snap poll (held just after the re-drawing of constituency boundaries, no less) may not allow time to do so comprehensively.

Some people may not get even a shot at voting. The electoral register is updated every year, with the new list coming into force on December 1st. Those who change address in the meantime can register ad hoc with their local councils, but only by special request. Mr Turner reckons that between 10% and 15% of the register changes each year, so an election held in November could leave more than 1m people disenfranchised. Labour has special reason to worry about this. “Churn” is greatest in cities, where the young and footloose move all the time—and where Labour is strongest.

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Conservative Party conference

The shock of the new

Oct 4th 2007 | BLACKPOOL
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The Tories have yet to decide whether it is enough to talk the talk

David Cameron

THE last time the Conservatives held their annual conference in Blackpool, in 2005, the faded glory of the town was a useful metaphor for a party whose best days seemed behind it. But David Cameron used the occasion to re-launch the party he now leads with a rousing speech urging modernisation. The Tories would have to move to the centre ground, he indicated, and work to lose their image as bigots and defenders of privilege.

Two years on, and the Tories do indeed show signs of change. The party favours civil partnerships for gay couples. The patient's passport, a proposal to let people buy private medical care, has been ditched. Support for new selective grammar schools, popular among party activists but not with the wider electorate, has met the same fate. In foreign policy, Tories now have something to say about the world outside Gibraltar and Zimbabwe.

The party also looks a bit more like the country it wants to serve. A third of the candidates selected to fight the next election are women. Sayeeda Warsi, a Muslim woman who serves in the shadow cabinet, shone at the conference, and a glance around the hall suggested that the average age of party activists is dropping.

Yet there were also signs that the party's drive to the centre may have run its course. What really galvanised the faithful was a proposal to raise the threshold at which inheritance tax is levied from £300,000 to £1m, paid for by a tax on non-domiciled foreigners (see article). It won plaudits from the right-wing press. But Labour will not be alone in observing that Mr Cameron had promised that his policies would be judged according to their effect on the poor and his flagship tax proposal does nothing for the worst-off.

This will be hard for the Tories to rebut, for the average house in Britain still costs about £100,000 less than the current inheritance-tax threshold. Many Tory members are too well-off to grasp how most Britons live (a participant at one fringe event said it was impossible to buy a one-bedroom flat in London for less than £250,000, which will be news to some in that city). The shadow cabinet cannot afford to seem similarly out of touch.

There were other signs too that modernisation is losing momentum. Two of the best-received speeches were by right-wingers: David Davis, the shadow home secretary, and Liam Fox, the shadow defence secretary. Mr Cameron's own speech, skilfully delivered on October 3rd without script or autocue, revived Europe, welfare reform and immigration as Tory themes. The environment, at the heart of Mr Cameron's speeches and stunts during his first year as leader, got only a few lines.

For the more grizzled Westminster commentators, short-term political calculation is behind all this. It was hoped that rousing the core Tory vote would be enough to discourage Gordon Brown from calling a snap election that Mr Cameron, for all his outward confidence, was likely to lose.

Some advance another theory. The founders of New Labour, whatever their personal clashes, agreed that their party needed to overhaul both policy and presentation. Tory modernisation has been shrouded in ambiguity from the outset. Some thought it enough to re-brand the party, transforming the way it spoke to voters but only tinkering with policy. Others argued that substance too must change.

It may be that the Tories, having delayed until now the choice between these two courses, are settling for the former. That is not self-evidently foolish: research after the 2005 election found that many of the party's policies were popular—until respondents learned they were Conservative. Now that the brand has been improved, many think the Tories must keep offering voters a clear alternative to Labour's centrist

policies—compassionately presented—if they are to be elected.

Those yearning for more modernisation, however, regard recent polls showing the Tories well behind Labour as proof that they must attack the centre ground. For the Tories want power, not just survival. Whether they get it—not in the next election, perhaps, but in the one after that—may depend on whether voters believe the change they have undergone has gone far enough.

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Taxing rich foreigners

One tax to bind them

Oct 4th 2007
From The Economist print edition

A loophole comes under political attack

LITTLE riles the British more than unfair play. Most vexing of late is the realisation that ever more wealthy foreigners (and quite a few natives to boot) are using a crafty loophole to avoid paying tax on foreign income and the gains from selling assets held abroad.

In most countries residents are taxed on their worldwide income. Residence is assessed by objective criteria: how long someone has lived in the country, for instance. But in Britain foreigners may claim residence and citizenship yet avoid paying tax on foreign income and capital gains by declaring themselves “non-domiciled”, asserting a “long-term connection” with another country.

The issue spilled into open political battle on October 1st, when George Osborne, the Tory shadow chancellor, proposed a flat tax of £25,000 ($50,000) a year on everyone claiming the exemption. The new tax, he said, would fund the £3.5 billion cost of cutting the burdens of inheritance tax and stamp duty, a tax levied on property transactions. Mr Osborne's crackdown looks timely: resentment about the rule has been building for many months, for two reasons.

The first is that an anachronism which once seemed to apply only to a few Greek shipowners or foreign oilmen is now finding wider use among the lawyers and bankers who keep the City of London's wheels turning. In 2002 about 65,000 people were non-domiciled residents. By the last count, in 2005, that had grown to 112,000. The Conservative Party thinks the figure may now be as high as 150,000.

The second reason is that the loophole, originally meant to apply only to foreign income, is now used to shelter earnings that would otherwise be considered British. Private-equity moguls, for example, can arrange to hold their personal investments in British takeover targets through offshore trusts, thus reducing to zero what little tax liability other loopholes left them with.

Mr Osborne may be optimistic in estimating that his measure would raise £3.5 billion (the Labour Party argues it will produce just £650m) but perhaps not by all that much. Bill Dodwell, head of tax policy at Deloitte, an accounting firm, reckons the figure is not a million miles from the mark. Others argue for a more nuanced approach. Caroline Garnham, a lawyer, says Britain could learn from Switzerland, where foreigners negotiate how much tax they will pay in exchange for the right to live there.

Still, debating the detail of a reform is easier than pressing through change. One reason why Gordon Brown has done nothing over the past decade is his reluctance to weaken the City of London by driving away foreign financial talent. Yet it is remarkable that the Tories—the historical party of business—should take the initiative. Tory strategists believe that the non-domicile rule is so patently unfair that the electorate will turn a deaf ear to Labour's attempt to undermine their sums.

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Crossrail

At long last

Oct 4th 2007
From The Economist print edition

Another prime minister, another promise—but this one may be honoured

Get article background

LONDON'S Crossrail project—a £16 billion ($32 billion) plan to build an east-west rail link across the crowded city—is something of a standing joke in politics. First officially proposed by Margaret Thatcher in 1989, it was subsequently endorsed by each of her three successors. All the main political parties are in favour, as are most of London's lobby groups. Yet, after 18 years of prevarication, rows and ever-more-packed public transport, not a single clod of earth has been turned.

Now, at last, there may be movement. On October 1st Gordon Brown gave his backing to the scheme, provided that London businesses were prepared to pay their share of the construction costs. And that, of course, is precisely what has always been the rub.

Despite near-unanimous agreement that choked-up London needs Crossrail, no government has ever been willing to pay the full whack for it. The plan is for a big chunk of the money to come from a combination of a loan secured against future ticket receipts, voluntary donations from the scheme's beneficiaries (such as BAA, which operates Heathrow airport, and Canary Wharf, a property developer responsible for London's second financial hub, in the Isle of Dogs) and a special tax on all but the smallest London businesses.

Such a compromise annoys virtually everybody. Non-Londoners grumble that their taxes will be spent for the benefit of wealthy City slickers. Londoners retort that their city pays more in taxes than it gets back in spending, and that local funding for Crossrail is odd when almost all big infrastructure projects have been financed with central-government cash. But now it seems that broad financial agreement has been reached.

Companies with deep pockets, such as BAA and Canary Wharf, have agreed on “voluntary” contributions. The City of London, the Square Mile's local authority, held out a little longer. Eventually, in a closed meeting on the evening of October 2nd, the City's councillors agreed to come up with a sum believed to be between £250m and £400m over and above the special tax paid by firms in the capital. The City's capitulation came in return—or so the rumours go—for an increase in its grant from central government. In theory, that leaves the way more or less clear for Crossrail to go ahead. An announcement was expected as *The Economist* went to press.

Why the sudden accord? The transport case for Crossrail gets more convincing every year. London Underground regularly breaks its own records for the number of passengers carried on its sardine-tin

trains. Road-traffic levels in central London are rising again after dropping when congestion charging was introduced in 2003. And with the city's population projected to rise from 7.5m today to 8.1m by 2016, the problem can only get worse. The economic case, if less cut-and-dried, is also accepted by most. Crossrail's backers reckon their project will bring £30 billion of benefits to Britain over its lifetime by persuading more foreign firms to locate in London and saving time for existing commuters. Not building it, they say, costs the economy £1.5 billion a year.

But politics is likely to weigh more heavily than either of these factors. As a Scottish Labour politician, the argument runs, Mr Brown needs something to keep Home Counties voters on his side. With speculation about an early election swirling, announcing a big, solid infrastructure project seems a perfect way for Mr Brown to distinguish himself from the Conservatives. Their leader, David Cameron, has styled himself the heir to Tony Blair, but he has been wrong-footed by Mr Brown's focus on grittier matters. Revealing firm progress on Crossrail would be another way for Mr Brown to underline this difference.

Yet even with the money problems solved, it is not clear when the trains might start running. Construction firms say that massive works for the 2012 Olympic Games will suck up thousands of builders, causing costs to soar. Optimists reckon parts of the line could be finished by 2015. But Crossrail's long and ignoble history of delays inspires caution. “I'll believe it's really going ahead,” says Tony Travers, an economist and Crossrail-watcher at the London School of Economics, “when I see the queen with a spade in her hand.”

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De Menezes and Diana

A tale of two inquests

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From The Economist print edition

An unresolved tragedy and a drawn-out farce

LONDON'S two most famous courts were in session this week with two very different cases. Deep in the Gothic bowels of the High Court, a jury heard the story of a glamorous life that ended in an apparently unremarkable death. A mile to the east, at the Old Bailey, another jury heard the case of a man who, until his extraordinary killing, was unknown.

Princess Diana died ten years ago. But the British inquest into the death of her and her lover, Dodi al Fayed, in a Paris car crash, got properly under way only on October 2nd. The £10m hearing is the latest—and, taxpayers must hope, final—episode in a long series of investigations in France and Britain that have failed to unearth anything out of the ordinary.

A French magistrates' report in 1999 blamed the couple's driver, Henri Paul, who had been driving over the speed limit, high on alcohol and prescription drugs. For four years Dodi's father, Mohamed al Fayed (who believes the crash was arranged by the Duke of Edinburgh and the British secret services), launched a series of appeals. A British inquest eventually kicked off in 2004 but was adjourned while the Metropolitan Police carried out its own investigation, which concluded in December 2006 that the affair had indeed been an accident. The inquest recommenced—and then stalled, while Mr al Fayed successfully appealed to have the case heard by a jury. Under way again at last, it is expected to last for six months.

At the Old Bailey, a case based on the death of Jean Charles de Menezes is due to take something more like six weeks. De Menezes, a 27-year-old Brazilian electrician, was pinned down and shot dead by police in a Tube carriage at Stockwell station, south London, in 2005. The officers had mistaken him for Hussain Osman, an Ethiopia-born Islamist who had planted a dud bomb at a different Tube station the previous day. It was de Menezes's misfortune to live in the same block of flats as the failed bomber, who in July was handed a life sentence for his failed plot.

In contrast to the endless details of the Diana saga, little is known about de Menezes's death. The first report of the Independent Police Complaints Commission (IPCC) has been leaked but not published. Based on its findings, prosecutors have decided they cannot charge any individual with the killing. The lack of a single responsible figure also prevents them from charging the police with a serious offence such as corporate manslaughter. The unhappy compromise, which began on October 1st, is a prosecution under the Health and Safety at Work Act, a law more commonly deployed against dodgy builders and whose maximum penalty is a fine.

Lame though it sounds, the case is at least squeezing out more details of the tragedy. The police firearms team, which was supposed to accompany surveillance officers at 6.00am to the block of flats where de Menezes lived, had still not shown up by the time the young man left at 9.30am (and had allegedly stopped on the way to buy petrol). The atmosphere in the police control room is said to have been “noisy and chaotic”, full of officers who had no business there and would not leave when asked. Ironically, it is this very chaos that may have saved senior officers from prosecution, since it is unclear who was responsible for what.

A proper inquest will follow, allowing the de Menezes family to ask their own questions and perhaps to scrape together more details. They hope that a verdict of unlawful killing could persuade prosecutors to try again to find someone responsible for it. Failing that, a full public inquiry could shed more light on the police's shoot-to-kill policy, the subsequent cover-up and the seeming weakness of the IPCC faced with an unco-operative force.

The victim's family is fighting an uphill battle. No police officer has ever been successfully prosecuted for committing murder or manslaughter in the course of the job. But it should soon be easier to hold officers accountable. A new corporate-manslaughter bill, enacted in July, makes it possible to convict companies without proving the culpability of an individual. Much against the government's inclination, the act will be

extended in three years' time to police and prisons. It is too late for the de Menezes family, but it may help others get justice.

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Interest rates

Holding operation

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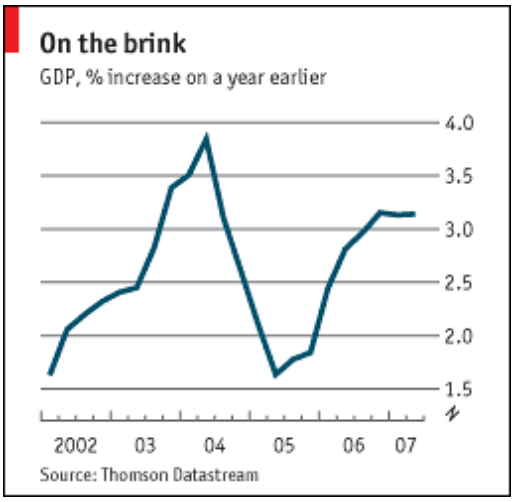
From The Economist print edition

Why the Bank of England may cut rates next month

FORGET BC and AD. For the financial markets, the date dividing two eras is August 9th, when the financial markets seized up. Before then the City was sure that the base rate would rise this autumn to 6%. Instead, the Bank of England's rate-setters decided for the third month running to keep it at 5.75%, when they met on October 4th. As far as the City is concerned, the question now is not whether the base rate is coming down but when.

The do-nothing decision by the bank's monetary-policy committee (MPC) may seem cautious, given that in America the Federal Reserve has already cut interest rates by half a percentage point. But the American economy has been weakening because of a sharp downturn in the housing market. In contrast, the British economy has been in fine fettle until this summer, not least because of the continuing buoyancy of house prices.

The momentum of GDP growth before the financial turmoil of the past two months was underlined in recent official figures, which tweaked it up from 3.0% to 3.1% in the year to the second quarter. When the number-crunchers have completed all their revisions, recent growth may turn out to have been as fast as 3.5%, according to the bank. That's uncomfortably higher than the trend rate of 2.5-2.75% at a time when the economy has been operating at around full capacity.



Already, however, there are signs that the economy is starting to slow. This week's surveys of purchasing managers indicated that the manufacturing and services sectors, though still performing well, weakened in September. A report from the Confederation of British Industry painted a particularly gloomy picture for the financial-services sector's prospects over the next three months.

The housing market has remained surprisingly perky, but strains are beginning to appear there too. The number of mortgages approved for house purchase declined from 115,000 in July to 109,000 in August. In another sign that the market is slowing, house prices fell last month by 0.6% according to HBOS, a bank.

More pain is likely, as credit conditions tighten because of the financial crisis. In the mortgage market, borrowers seeking two-year fixed-rate loans worth 95% of a home's value are now paying sharply more than those who need to finance only 75%. And companies have been hit hard: those taking out new loans at interest rates fixed for up to a year were charged 7.63% in August, up from 6.63% in June.

As a result, the economic outlook is darkening. According to *The Economist*'s poll of forecasters (see article), GDP growth is now expected to slow quite substantially, from 2.9% this year to 2.1% in 2008. The outcome could be even grimmer. Growth will slip to 1.4% next year, says CEBR, an outfit that keeps a close eye on the City, whose fortunes have taken a turn for the worse. As further evidence emerges that the economy is going to slow sharply, the MPC is likely to cut rates sooner rather than later. Relief may come as early as November.

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Bagehot

Triple or quits

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From The Economist print edition

Illustration by Steve O'Brien

Why David Cameron has less to fear from an autumn election than Gordon Brown

Gordon Brown

PINK in the sunset, the fairground rides at the end of Blackpool's piers look magically inviting. At night the famous illuminations throb in gaudy colour, lighting up the mini-Eiffel tower, Ferris wheel and roller-coasters on the eccentrically eclectic seafront. But in the sober light of day, the shabbiness is unavoidable. The attractions are primitive; the piers are decrepit; the food is terrible. The tastes of the punters who once thronged the promenade have moved on, but Blackpool hasn't.

More or less the same might be said for the Conservatives, who gathered this week at Blackpool's Winter Gardens (fake medieval hall, galleon-shaped bar, Moorish flourishes) for their annual conference. The braying squires, horsey women, bespectacled ideologues and aggrieved small businessmen are also eccentrically diverse, but not really in the way that David Cameron, the Tory leader, would like. For all the glitz, the vaunted compassion that Mr Cameron had tried to inculcate and the studied spontaneity of his big speech on October 3rd, the delegates were lit up mostly by the old-fashioned Tory attractions of tax cuts and Europe-bashing. Ten-odd points behind Labour in some polls, the Tories look ominously vulnerable to Gordon Brown's master-plan—which is to push them from picturesque quiescence towards total destruction.

For that is what the autumn election, which Mr Brown will probably call next week, will in part be about. Doubtless Mr Brown would like his own electoral mandate. Certainly he is keen to secure an extra couple of years in office, which a victory now would assure him. But the prize big enough to justify the risks involved in going to the country next month is the crippling, or even annihilation, of the Tories. And for all his strength and their apparent weakness, Mr Brown is unlikely to achieve it.

What rhymes with “Duncan Smith”?

“Mary, Lizzie, James the Vain, Charlie, Charlie, James Again”: schoolchildren learn rhymes to help them remember the sequence of British monarchs. Future political historians may have to think up ditties to help them remember the Tory leaders sacked after failing to dislodge Tony Blair (was it two bald ones or three?). The list of ex-leaders may soon include Mr Cameron. In a November poll, the Brownites hope, Labour will win the increased majority that its current poll lead seems to promise. The distressingly plausible Mr Cameron will get the boot, to be replaced by an unelectable right-winger—thus disqualifying the Tories from office for another decade. In the wilder Labour imaginings, the Tories back-stab and bicker themselves into oblivion.

That scenario ought to worry not only Tories, but also anyone who thinks that competitive politics is a good idea, or who doubts that Labour's record has been stellar enough to entitle it to govern in perpetuity. The prospect is not completely outlandish, and it is an intoxicating one for Labour. But it is more likely that Mr Brown himself will be damaged.

Even in the baldest times, at least 30% of Britain religiously votes Tory, or intends to. That block of instinctive conservatives is probably less tractable than the annihilationists hope. The British enthusiasm for chucking out governments has been unusually dormant in the last thirty years, but it has not died entirely. As well as those structural reasons for doubting that the Tories are conclusively doomed, there are others for believing that these particular Tories might do better than disastrously.

Before the slide of the past few months, Mr Cameron was regarded by many of his opponents as the most talented Tory leader since Margaret Thatcher. A televised—and highly personalised—election campaign will acquaint more voters with those talents. Meanwhile, Mr Brown's “bounce” has been propelled by his self-portrayal as a national leader above mere party. It will be tough to maintain that image in the partisan warfare of an election campaign (it has already been tarnished by a row this week over his opportunistically timed announcement of troop reductions in Iraq). And so on.

Of course, Mr Cameron will probably lose. But he might lose well enough to keep his job. The earliness of the election may even help him keep it: he will be able to argue that cutting Mr Brown's majority in the House of Commons is a creditable performance after only two years as leader, and a vindication of his “modernising” strategy. The cuts in inheritance tax and stamp duty announced this week by George Osborne, the boyishly clever shadow chancellor, were aimed at the marginal seats in the south-east that the Tories need to take for that minimum goal. And a hung parliament, even if Mr Brown stayed in Downing Street, would be a triumph. In two years' time, the bar set for Mr Cameron by his demanding, intermittently fractious party would be much higher. By trying to crush Mr Cameron, in other words, Mr Brown might inadvertently nurture him.

For the prime minister himself, in an election of his choosing, the maths are different. A hung parliament would be a catastrophe. An unworkably small majority would be a disaster. Losing more than a few seats would be embarrassing. Whispers about his judgment—and his leadership—would begin.

Yet if he backs down now, Mr Brown risks being seen as “frit”, a quaint term of Lady Thatcher's that buzzed around Blackpool, along with “change”, “dogwhistling” and “referendum”. He may now regret letting the election fever reach quite this pitch. For his part—and for all the “bring it on” bravado of his speech, and the cocooned defiance of his conference—Mr Cameron would surely prefer Mr Brown to “bottle it”, as Mr Osborne put it. The leader of the opposition has to demand an election, explained one senior Tory, just as the pope has to profess belief in God—except that the pope probably means it. But if there is an election, Mr Brown should be the more worried man. He will have staked everything on a long-odds bet that he didn't need to make.

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Cities and natural disasters

Some hard talk about towns

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From The Economist print edition

AFP

The death toll from the catastrophes that strike cities doesn't have to keep climbing

IT ISN'T just an urban myth: life in a city really is getting more dangerous, and the sources of peril are not just human ones like muggers and reckless motorists. A report by UN-Habitat, an agency responsible for human settlements, says the number of natural disasters affecting urban populations has risen four-fold since 1975.

Some of the reasons are obvious, others less so. As the world's population grows, people are crowding into mega-metropolises, where life's risks are horribly concentrated. The after-effects of a natural disaster can be especially dire in a vast, densely-packed area where sewers fail and disease spreads.

At a pace that no urban planner can control, slums spring up in disaster-prone areas—such as steep slopes, which are prone to floods, mudslides or particularly severe damage in an earthquake. Many of the world's cities are located on coasts or rivers where the effects of climate change and extreme weather events, from cyclones to heatwaves to droughts, are brutally and increasingly felt. Economic dislocation and human pain are also caused by events (like recent floods in the Indian city of Kolkata, see above) that are too small to grab global headlines.

But there is no reason for the sort of fatalism that regards disasters, and their disproportionate effects on the urban poor, as something that has "always been with us" and will inexorably get worse.

Intelligent planning and regulation make a huge difference to the number of people who die when disaster strikes, says Anna Tibaijuka, UN-Habitat's executive director. In 1995 an earthquake in the Japanese city of Kobe killed 6,400 people; in 1999 a quake of similar magnitude in Turkey claimed over 17,000 lives. Corrupt local bureaucracies and slapdash building pushed up the Turkish toll.

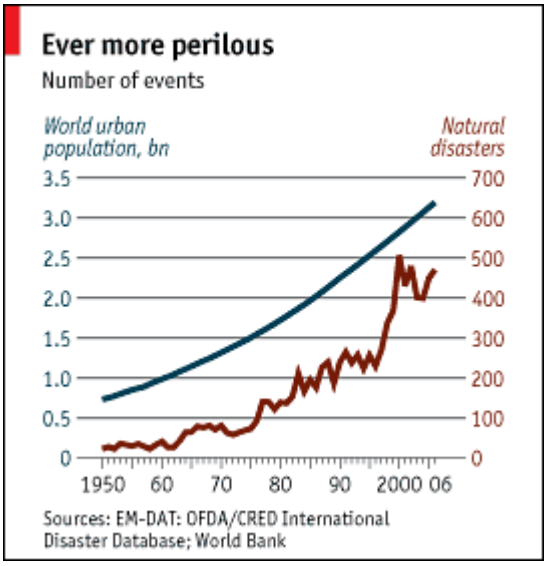
The Indian Ocean tsunami of 2004, which killed at least 230,000 people, would have been a tragedy whatever the level of preparedness; but even when disaster strikes on a titanic scale, there are many factors within human control—a knowledgeable population, a good early-warning system and settlements built with disasters in mind—that can help to minimise the number of casualties.

In some places, says Saroj Jha, a disaster specialist at the World Bank, tragic events have been a spur to serious national efforts to learn lessons and make buildings and infrastructure more robust. Often this has benefits that go far beyond the

disaster-stricken area. He cites Turkey, India, Vietnam, Sri Lanka and Indonesia as countries that have learned from catastrophes. For example, after a quake in Gujarat which killed 20,000, India trained a small army of engineers, architects and builders to raise the quality of construction.

The World Bank has recently started to focus more on avoiding disasters, rather than just helping to respond to them. There is more awareness that disaster-prone projects—such as dams which could burst—are worse than a waste of money.

Given that events like earthquakes and tsunamis cannot be escaped, the bank is also doing more to help poor countries prepare for the worst. There are economic reasons for this, as well as humanitarian ones. Many vulnerable cities are big contributors to the surrounding country's GDP—so an urban disaster could wreck an entire national economy. These include Tehran (which produces 40% of national GDP), Dhaka (60%), Mexico City (40%), Seoul (50%) and Cairo (50%).



And some of these urban spaces are disasters waiting to occur. The Bangladeshi capital of Dhaka (with a population of 11.6m and rising) is built on alluvial terraces, exposed to flooding, earthquakes and rising seas. Tehran is in such an earthquake-prone area that some have suggested moving the entire city of 12m people. That will hardly happen; but better foundations could save countless lives if—or when—an earthquake strikes.

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Civil liberties: detention without trial

The stuff of nightmares

Oct 4th 2007
From The Economist print edition

Judges and parliamentarians are restraining the zeal of governments who want a free hand to fight terror. The third in our series

Reuters

Guantánamo: where rights are shackled

HAULED before a military tribunal at the American naval base in Guantánamo Bay, the detainee, picked up in Afghanistan, asked why he was being held. For associating with a member of al-Qaeda, he was told. Give me his name, the detainee demanded. The tribunal's president said he didn't know it. Nor did any of the tribunal's other members. “How can I respond to this?” the detainee cried before being taken back to his cell to continue his detention, perhaps for the rest of his life.

This Kafkaesque story was related this summer by Arlen Specter, the ranking Republican on the Senate Judiciary Committee, in support of a bill he and Patrick Leahy, the committee's Democratic chairman, were co-sponsoring to restore *habeas corpus* rights to Guantánamo's detainees. Most have been held for nearly six years without charge, without access to a lawyer or any indication of when, if ever, they might be released. The Pentagon has said they could be held for the duration of the (open-ended) “global war on terror”.

Guantánamo has become a byword for the Bush administration's gung-ho reaction to the terror attacks of September 2001. In Britain, too, the government has sought new powers to tackle Islamist terrorism, even if these seemed to offend ancient liberties. But the story is not over yet. It could turn into a tale not of liberties being frayed, but of democracy's underlying strength. For, in both America and Britain, the doctrine of the balance of powers has passed a test. The executive branch made a grab for more authority; but courts and legislators have tried hard to push back.

Freedom from arbitrary arrest and detention, coupled with the right to challenge it in an independent court—known as *habeas corpus* in common-law countries like Britain and America—are among the civilised world's most sacred and ancient liberties, going back to medieval times. But these days, there is more talk of pre-emption and “preventive detention”, even in democracies. “You can't allow somebody to commit the crime before you detain them,” said Condoleezza Rice, the secretary of state, when asked about America's secret “renditions” programme for suspected terrorists.

What the public safety requires

Under the American constitution, *habeas corpus* may not be suspended except when “in cases of rebellion or invasion, the public safety may require it”. And only very rarely has it been suspended. Abraham Lincoln did so during the civil war, but was rebuked by the courts. And the internment of 120,000 people of Japanese descent, two-thirds of them American citizens, in the second world war, was lawful but is now viewed as a shameful misdeed.

Britain likewise suspended *habeas corpus* in the second world war to allow it to detain around 1,000 suspected fascists. All were released after three years. During the “troubles” in Northern Ireland in the early 1970s, nearly 2,000 suspected extremists were interned. But the practice was scrapped in 1975, as it was clearly fuelling support for terrorism—just as Guantánamo is doing now.

George Bush chose the American naval base in Cuba as the detention centre for those picked up in his war on terror because officials believed—falsely as it turned out—Guantánamo was beyond the reach of domestic and international law. If the detainees had been held on American soil, they could have claimed the same rights as ordinary American citizens, including a right to due process, to apply for asylum and

to sue the American government for any alleged wrongs.

From the outset, the 775 or so men and boys (some as young as 13) sent by Mr Bush to Guantánamo were branded as guilty. Donald Rumsfeld, the former defence secretary, described them as “hard-core, well-trained terrorists” who, if released, would simply “return to the fight and continue to kill innocent men, women and children”. The Pentagon says that all were “caught in the battlefield”. But many were given to the Americans by Afghan bounty-seekers; others were seized as far away as Bosnia and Zambia.

Mr Bush claims that, under international law, parties to an armed conflict may hold enemy combatants “for the duration of active hostilities”. This is correct. Nor is “unlawful enemy combatant” a term he invented. In the Geneva Conventions, it describes a foe who is not a member of official armed forces or an organised resistance movement, does not carry arms openly, wears no uniform or other distinctive sign, and refuses to heed the laws of war. As such, he fails to qualify for the rights of a prisoner of war. But, contrary to what the administration first claimed, he is entitled to some protections, including humane treatment and, if charged, to a fair trial by a “regularly constituted court”.

But is America's war on terror a real war in the legal sense? If not, then the detainees should be treated as ordinary criminal suspects. This is the path that most European countries have chosen. Even if it could be deemed a real war, it is clearly unlike an ordinary state conflict: it has neither a definable end nor even an identifiable enemy with whom to sue for peace. It could last for decades.

Meanwhile, dozens, perhaps hundreds, of detainees are apparently to be left to rot in their cages—if not in Guantánamo, which Mr Bush says he wants to close—then somewhere else. America has also engaged in so-called “extraordinary rendition”—the abduction of suspected terrorists to face not justice, but harsh interrogation, perhaps torture, in a third country. Up to 100 nameless “high-value” suspects are believed to have been seized by CIA agents and then transferred to secret jails, some never to resurface. Around 15 have recently been transferred to Guantánamo, where they may or may not face trial. But most of the 330-odd detainees remaining at the camp may never be charged or tried. The Pentagon says it hopes eventually to put up to 80 detainees on trial for war crimes by special military commissions. Even if acquitted, they may still be held as enemy combatants for the rest of the “war”.

In Britain, all renditions have been outlawed since a Court of Appeal ruling in 1999 overturned the conviction of an Irish Republican, Peter Mullen, who had been spirited back to Britain from Zimbabwe. His abduction was described by the court as a “blatant and extremely serious failure to adhere to the rule of law”.

Britain has eroded liberties in other ways. Immediately after the September 11th attacks, the government brought in a law allowing it to hold indefinitely and without charge any foreigner deemed a national security risk—on the simple say-so of the home secretary. To do this, it had to opt out of parts of the European Convention on Human Rights, as is permitted “in time of war or other public emergency threatening the life of the nation”. None of the 45 other signatories has deemed such a step necessary.

Belmarsh prison in London, where most terror suspects were held, was dubbed “Britain's Guantánamo”—a bit unfairly. Britain never claimed to be in the midst of a war or to be holding “unlawful enemy combatants” with no legal rights. Its foreign detainees, totalling no more than 18, always had access to a lawyer and could challenge their detention before an independent tribunal, though they were not allowed to see classified evidence against them. The government said they were not being held indefinitely, just awaiting deportation. But as they could not be sent to their own countries (because they might be tortured), and no other state wanted them, the effect was the same.

The law lords say no

In December 2004 the House of Lords, Britain's highest court, judged this system to be incompatible with the European Convention. For Lord Scott, one of the law lords involved, indefinite detention on undisclosed grounds was “the stuff of nightmares”, reminiscent of a Stalinist regime. The law was duly scrapped. But it was replaced by new powers allowing the home secretary (not a judge) to impose an indefinitely renewable “control order”—including electronic tagging, a ban on phone and internet use, and strict curfews amounting at times to virtual house arrest—on any suspected terrorist, British or foreign.

The new system seems as riddled with problems as the old, and almost as unfair. In its latest report on control orders, in September, the Home Office said three of the 14 people subject to the regime had absconded. Several people have had their orders quashed by judges who again found the measures

incompatible with the European Convention. The government has appealed to the House of Lords, which is expected to pronounce later this month.

In the final months of Tony Blair's government, ministers said they were prepared to “take the nuclear option” and opt out of the convention again if the law lords' ruling went against them. That threat has not been repeated by the new prime minister, Gordon Brown. But he may yet try similar moves. He has already announced plans for a new anti-terrorist law—Britain's fifth since 2000. Among his proposals is an extension of the maximum time a suspected terrorist can be held without charge from 28 days, already the longest in the West, to 56 days. Most democracies allow no more than three days. France permits four; Greece six.

But no leader of a Western democracy has obtained a completely free hand in detaining people. America has seen a tug of war between the government and the courts, with many rounds. In June 2004, the Supreme Court ruled that *habeas corpus* remained available to everyone detained on American soil, unless explicitly suspended. The case involved Yaser Esam Hamdi, an American citizen being held as an unlawful enemy combatant on a naval brig in Virginia. Two years later, in a case involving a Guantánamo detainee, Salim Hamdan, the Supreme Court said the basic protections afforded to all wartime detainees under the Geneva Conventions applied to everyone, even to unlawful enemy combatants outside America.

The court also ruled that Mr Bush had exceeded his authority in setting up, without congressional approval, special military commissions to try some of the Guantánamo detainees. In response, the president pushed through the 2006 Military Commissions Act giving him just such authority. That law also stripped Guantánamo detainees of any vestige of *habeas corpus* rights, with retroactive effect. This seemed to dash the hopes of hundreds of Guantánamo detainees with challenges pending before American civilian courts. In April, that view appeared to be confirmed when the Supreme Court turned down, without comment, a *habeas corpus* petition from the above-mentioned Mr Hamdan. But in June it relented, agreeing to hear an almost identical case from another Guantánamo detainee. Many hope the Supreme Court will seize this opportunity to give a view on whether Mr Bush's “war on terror” is a real war.

The legislators strike back

Congress, too, is beginning to show its teeth, particularly now it is under Democratic control. Although Senator Specter's bipartisan bill to restore *habeas corpus* rights to Guantánamo detainees fell to a Republican filibuster on September 19th, it got the support of 56 senators, including four Republicans. Other bills pending before Congress seek the total closure of Guantánamo with the transfer of the detainees either to their home countries, if they do not present too big a threat and if those countries are willing to take them; or to a military prison in America.

In Britain, too, Parliament has baulked at some of the government's demands. In 2005, when Mr Blair sought to push through a bill raising the time a suspected terrorist could be detained from 14 to 90 days, his backbenchers revolted, eventually settling on the compromise of 28 days, with regular judicial oversight. Some British officials have been looking with envy at civil-law countries like France, where the criminal-justice system allows detention for months, even years, after a suspect has been formally “placed under investigation”, but not yet charged. Police can also continue to interrogate suspects during that time.

But most legal commentators believe that if the French model were copied in this area, an unbearable blow would be dealt to England's common-law system. And despite the fears of civil libertarians, there are still judges and legislators who think that system worth preserving.

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Mobile advertising

The next big thing

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Illustration by Claudio Munoz

Marketers hail the mobile phone as advertising's promised land

ADVERTISING on mobile phones is a tiny business. Last year spending on mobile ads was $871m worldwide according to Informa Telecoms & Media, a research firm, compared with $24 billion spent on internet advertising and $450 billion spent on all advertising. But marketing wizards are beginning to talk about it with the sort of hyperbole they normally reserve for products they are paid to sell. It is destined, some say, to supplant not only internet advertising, the latest fad, but also television, radio, print and billboards, the four traditional pillars of the business.

At the moment, most mobile advertising takes the form of text messages. But telecoms firms are also beginning to deliver ads to handsets alongside video clips, web pages, and music and game downloads, through mobiles that are nifty enough to permit such things. Informa forecasts that annual expenditure will reach $11.4 billion by 2011. Other analysts predict the market will be as big as $20 billion by then.

The 2.5 billion mobile phones around the world can potentially reach a much bigger audience than the planet's billion or so personal computers. The number of mobile phones in use is also growing much faster than the number of computers, especially in poorer countries. Better yet, most people carry their mobile with them everywhere—something that cannot be said of television or computers.

Yet the biggest selling point of mobile ads is what marketing types call “relevance”. Advertisers believe that about half of all traditional advertising does not reach the right audience. Less effort (and money) is wasted with online advertising: half of it is sold on a “pay-per-click” basis, which means advertisers pay only when consumers click on an ad. But mobile advertising through text messages is the most focused: if marketers use mobile firms' profiles of their customers cleverly enough, they can tailor their advertisements to match each subscriber's habits.

In September Blyk, a new mobile operator, launched a service in Britain that aims to do just that. It offers subscribers 217 free text messages and 43 free minutes of voice calls per month as long as they agree to receive six advertisements by text message every day. To sign up for the service, customers must fill out a questionnaire about their hobbies and habits. So advertisers can target their messages very precisely. “Britain is the largest, but also the trickiest European ad market, so if it works here it will work everywhere,” says Pekka Ala-Pietila, chief executive and one of the founders of Blyk.

Last year America's Virgin Mobile tried something similar with its “Sugar Mama” programme, which offers subscribers the choice between receiving an ad via text message or viewing a 45-second advertisement when browsing the internet in exchange for one free minute of talk time. Those who spend five minutes

filling out a questionnaire online get five more minutes. Sugar Mama is proving popular: at the end of August Ultramercial, the company that manages the scheme, reported that Virgin Mobile had given away more than 10m free minutes.

Vodafone, a big mobile operator based in Britain, sees mobile advertising as a potentially lucrative source of additional income. For the time being, most of the ads on its network are still text messages, although it has begun displaying ads on Vodafone live!, its mobile internet homepage, through which subscribers access the internet and download videos and music. Vodafone is also running several pilots, says Richard Saggers, the head of its mobile advertising unit, in which subscribers receive free content in exchange for viewing ads. Earlier this year, subscribers in Britain were given the option of downloading footage from “Big Brother”, a reality-TV show, in exchange for viewing a promotional video clip. The firm has also offered free video games punctuated with ads to customers in Greece, and free text messages to Czech students who agree to accept ads in the same format.

Most mobile advertising strategies now rely on text messages, since few customers have taken to more elaborate services that allow them to download music, games and videos and to surf the web. Only 12% of subscribers in America and western Europe used their mobiles to access the internet at the end of 2006. Most people think mobile screens are too small for watching TV programmes or playing games, although newer models, such as Apple's iPhone, boast bigger and brighter screens.

That is not the only problem. While consumers are used to ads on television and radio, they consider their mobiles a more personal device. A flood of advertising might offend its audience, and thus undermine its own value. Tolerance of advertising also differs from one market to another. In the Middle East, for example, unsolicited text messages are quite common, and do not prompt many complaints. But subscribers might not prove so open-minded in Europe or America.

Another hitch, says Nicky Walton-Flynn of Informa, is that operators have lots of databases with information about their clients' habits that would be of great interest to advertisers. But privacy laws may prevent them from sharing it. Moreover, advertisers, operators and middlemen have not agreed a common format for this information, nor worked out how to share the revenue it might yield.

Some think these obstacles will confine mobile advertising to a niche for years to come. But others see a whole new world of possibilities, as more people use their phones to access the internet and consumers grow used to the intrusion. Mobile phones, some of which are now equipped with satellite-positioning technology (see article), could be used to alert people to the charms of stores or restaurants they are walking or driving past.

Tying ads to online searches from mobile phones is another potential goldmine. A subscriber typing in “pizza” for instance, could receive ads for nearby pizza parlours along with his generic search results. Such a customer, mobile operators hope, is likely to be more grateful than annoyed by the intrusion. What could be more relevant than that?

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Satellite navigation

Location, location, location

Oct 4th 2007 | AMSTERDAM
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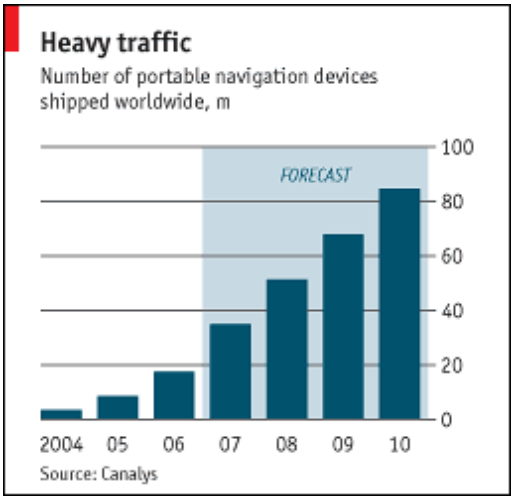
Where is the navigation industry heading?



MEN, the stereotype has it, never ask for directions. Now many of them have an excuse, in the form of a portable navigation device (PND). Nearly 35m of these hand-held or dashboard-mounted units will be sold around the world this year, twice as many as in 2006 (see chart), making personal navigation one of the fastest-growing areas in consumer electronics. The latest versions of these gadgets do more than simply show the stubborn or shy the way. The industry is beginning to focus on the services PNDs could provide, prompting a scramble for the ownership of the digital maps they use.

Proof of this shift came on October 1st, when Nokia, the world's largest mobile-phone maker, said that it would acquire Navteq, the world's biggest maker of digital maps, for €5.7 billion ($8.1 billion) in cash—a heady sum for a company with only $362m in revenues and $71m in net income in the first half of this year. In July, TomTom, a leading PND vendor from the Netherlands, announced plans to buy Tele Atlas, the next biggest mapmaker, for €1.8 billion.

Between them, TomTom and its main rival, an American firm called Garmin, make nearly half of all PNDs. Their margins on them are almost 50%. But their dominance and profitability is unlikely to persist, says Chris Jones of Canalys, a consultancy. Nokia is already making its presence felt with phones that can pick up signals from global positioning system (GPS) satellites and plans to add this feature to more models soon. Start-ups such as Dash, a Silicon Valley firm, could also shake up the market. Prices for PNDs have already dropped, from around $630 on average in 2005, to $400 now.

This rapid deflation has prompted speculation that PNDs will soon become a commodity. Naturally, both TomTom and Garmin reject the idea. They argue that navigation systems are complex beasts that require a tight integration of hardware and software to make them easy to use. This is why Garmin invests more than $150m annually in R&D, says Kevin Rauckman, the firm's chief financial officer.

Still, most of the innovation is now occurring in supplementary services rather than in basic navigation system, argues Harold Goddijn, TomTom's boss. That is where his firm has placed its big bets. Drivers in the Netherlands and Britain, for instance, will soon be able to subscribe to real-time traffic information that will allow their PNDs to steer around traffic jams. To provide prompter warnings of congestion, TomTom has teamed up with Vodafone, a mobile-phone carrier. It can tell how quickly cars are moving by the speed with which phones on its network switch from one transmission cell to the next.

Once PNDs can send and receive data or, conversely, mobile phones come equipped with a receiver for GPS signals, all kinds of services become possible. Users of Garmin's products can already check fuel prices at the petrol stations that appear on their maps and screening times at cinemas. Nokia, for its part, wants to target pedestrians. One of the services the Finnish company is planning to introduce is a system to help friends find one another: if any are nearby, their names will pop up on a digital map (presumably, those wishing to avoid unwanted friends and lovers will have to disable this feature). Another offering will be geo-tagging: users of Nokia phones will be able, for instance, to write a review of restaurants that others can read as they peer through the window.

To date, digital mapmaking has not been very profitable. Nokia and TomTom both hope that they can cut costs by tapping enthusiastic subscribers to update and improve their maps. That is quite a task: every year, some detail changes on 15% of all roads, be it a new name or a change in traffic flow. Navteq alone employs 700 “geographic analysts” to keep abreast of things. TomTom recently launched a service called

MapShare, which allows its users to suggest corrections to its maps. Clever software and wary editors then decide which suggestions to adopt. The firm expects lots of feedback. Even before it launched the service, it received 16,000 corrections each month, but had no effective way of dealing with them.

Yet the chief rationale for Nokia and TomTom's purchases is strategic. Both seem to think that they need to be in control of the maps they use to keep a big share of the revenue generated by location-based services. At any rate, they want to ensure that the tools of their trade do not fall into the hands of predatory giants such as Microsoft and Google. The latter already buys maps from both Navteq and Tele Atlas and lets users annotate them, and is beginning to send out its own geographic analysts.

For now, both Nokia and TomTom are likely to stick to their promise to keep selling the same maps they use themselves to competitors such as Google. After all, neither wants to reduce the paltry profits of their new purchases by jettisoning big clients. But in the long run, the temptation to raise prices and to give their own PNDs and services privileged access to maps may prove overwhelming.

Some fear that the world may end up with a digital map monopoly, as users migrate to the provider with the most comprehensive data and then further strengthen its position by adding information of their own. Such worries have given rise to a nascent “open-map” movement. Owners of PNDs can record their wanderings, collect information about their routes and upload the data to a website called OpenStreetMap. In time, such contributions could create a detailed, free map of the world. If so, TomTom's and Nokia's acquisitions would look very overpriced.

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Mining royalties

What's mined is yours

Oct 4th 2007
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Prospecting for riches in the tax code

THE discovery of rich seams of metal in remote places used to bring prospectors rushing in the hope of making their fortunes. Now a different sort of scramble is under way, as governments around the world try to lay their hands on a bigger share of the proceeds of mining. Metals prices have soared in recent years, thanks mainly to growing demand from China and other booming economies. That has lifted mining firms' profits—and drawn the attention of finance ministers.

Several African countries, for example, are rewriting the rules for mining firms. The latest victim is AngloGold Ashanti, a South African gold-mining concern, which has agreed to an overhaul of the taxes it pays in Tanzania to speed the flow of cash from its mines to the government's coffers. Canada's Barrick Gold and Australia's Resolute have agreed to similar arrangements in Tanzania, while Guinea also wants to amend a previous deal with AngloGold.

Reuters

He wants more buck for his bang

Zambia, meanwhile, plans to cash in on the stratospheric price of copper by renegotiating the generous terms it gave to foreign firms when it privatised its copper mines in 2000. Then the price was low. Although these investors rescued an industry close to collapse, Zambia now wants to increase royalties and other taxes. Congo said in April that it was reviewing all mining contracts. And Indonesia wants America's Freeport McMoran to pay higher royalties at its huge Grasberg mine.

Latin America is an exemplar for the newly assertive nations. In 2004 the governments of Chile and Peru imposed new royalties. Last year Peru convinced mining firms to spend some $780m on social programmes over five years. Now Bolivia is contemplating nationalising some mines and Ecuador is threatening to review concessions. And other troubles lurk for big mining companies in the region. Workers, keen to redivide the spoils, are threatening strikes in Peru and last year disrupted production at Chile's vast Escondida mine, owned by Australia's BHP Billiton, for 25 days before securing a lavish pay rise.

Governments intent on reworking contracts or imposing new taxes clearly feel that they have the upper hand at the moment. When prices were depressed and profits scarce foreign firms had to be lured with generous terms that now rankle. But strong growth in Asia should keep metals prices high for years, while a shortage of engineers and equipment is hampering investment in new mines. So mining firms are likely to swallow their pride and agree to any deals that allow them to continue to rake in profits.

But to invest in mines with decades-long lifespans, mining firms want enduring tax and regulatory regimes. As metals prices rise and fall, they argue, they will sometimes seem to be doing best out of any given regime, while at other times, governments will benefit most—it's the luck of the draw. They also claim that countries that acquire a reputation for moving the goalposts may find that when times are tougher investors will think twice before agreeing to new deals—although if that were really true, they would have left many of the countries concerned long ago.

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Health care

The vault is open

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Microsoft makes its big move into health care

BACK in 2000, Steve Ballmer, Microsoft's chief executive, described a grand vision for the future of health care. One day, he said, everyone would have a secure and private website on the internet on which their doctors could post their "scans, lab results, test results, visit minutes" and the like, and to which the owner could grant certain people access, to view some or all of that information.

His ideas met with guffaws from the old lags of the industry, who have seen many fancy schemes for electronic medical records fall flat. America's health sector is simply too balkanised and too paper-based to stitch together easily in digital form. Google, Intel, Revolution (a firm started by Steve Case, a founder of AOL) and other Silicon Valley firms have all tried to do this, with little success. Even Mr Ballmer conceded back then that he was searching for the "holy grail" of healthcare.

And yet, after years of frustration and furious development work, Microsoft now believes it has realised Mr Ballmer's dream. On October 4th, as *The Economist* went to press, the software giant was poised to unveil its new health-information product at a big event in Washington, DC. It is called the Health Vault, in keeping with Microsoft's promise to make storing data on the internet just as secure as keeping it in a bank.

Health Vault will store all its customers' health data, ranging from test results to doctors' reports to daily measurements of weight or blood pressure, online. Individuals then have access to those records any time, anywhere, via the internet—a great boon for those who travel a lot. Medical offices and hospitals who sign up for the service could easily send test results in digital form to the vault, and patients could authorise them in turn to have access to various, carefully circumscribed bits of their personal data.

Microsoft was also set to announce this week that several dozen manufacturers, hospitals and charities have signed up for Health Vault. Big names including the American heart, diabetes and lung associations, the NewYork-Presbyterian Hospital, and Omron and Texas Instruments, in addition to various firms devoted to the craze for "wellness", are all now on board, and are expected to announce products and services shortly.

If the software giant has really found a hacker-proof way of storing records online, then the benefits of Health Vault are clear. But use of the vaults will be free both for the individuals that sign up for them and for the vendors and doctors that provide services based on the information they contain. So how will Microsoft make any money?

Sean Nolan of Microsoft explains that the business model depends on one thing: targeted search. Microsoft is betting that people will use its Health Vault Search to find out about their ailments. This service relies on an approach known as "vertical search" which attempts to provide more relevant results than generalist search engines like Google and Yahoo! by specialising in a particular field. The firm's recent acquisition of Medstory, a vertical-search engine focusing on health care, has given it a boost in this area.

Health Vault's search engine would definitely work better than those of rival sites if it could examine users' health records and past queries, and thus provide the responses that are most relevant to each individual's situation. But in order to attract any users in the first place, Microsoft has promised to enforce strict privacy rules. These, says Mr Nolan, would preclude such data-mining.

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Chinese carmakers

Nyet

Oct 4th 2007 | HONG KONG
From The Economist print edition

Russia slams the door on Chinese car factories

THIS week saw two curious announcements concerning Russian cars. First, China's Xinhua news agency reported that Russia's Economic Development and Trade Commission had issued a decree forbidding foreign carmakers from building new plants. The next day Italy's Fiat elaborated plans to do just that, saying it would make 60,000 cars a year at a new factory in the Volga region in partnership with Severstal Auto, a Russian firm. The “decree”, it appears, applies only to manufacturers from China.

Seven Chinese car companies have so far applied for licences in Russia but only one of them, Chery Automobile, has been granted approval. Yet all their big American, European, Japanese and South Korean rivals have got the go-ahead; several are already making cars in Russia. Now there are reports that Russian carmakers are lobbying for Chery's licence to be revoked.

Another Chinese firm, Great Wall, first declared its intention to invest $40m in a plant in the region of Tatarstan 18 months ago. It says it remains in negotiations with the Russian authorities. But according to Xinhua, the decree will force it and the five other Chinese applicants to revisit their plans for Russia.

Part of the explanation may be doubts about the safety of Chinese cars. A video of China's best-selling car in Russia, the $9,000 Chery Amulet, collapsing as if made from cardboard when crash-tested by a Russian magazine has become a favourite on YouTube. Chinese cars have also performed poorly in German safety tests.

But Russia's rebuff may stem as much from Chinese carmakers' successes as from their failings. Until 2005 there were no exports of Chinese cars to Russia at all. This year, 120,000 vehicles are expected to arrive. In a country where 2.1m vehicles were sold last year, the Chinese manufacturers' volumes are still small. But, according to official figures, Chery's sales grew by 580% in the first eight months of 2007, to 24,000. Other foreign brands grew by an average 66%.

“Russia is one of the most promising markets for Great Wall,” Shang Yugui, a spokesman for the company, said this week. Unlike Western carmakers, Chinese ones compete head-on with Russia's indigenous manufacturers on price. That makes them really dangerous.

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Abu Dhabi

Media oasis

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An Arab statelet is spending huge sums to turn itself into a media hub

WHEN location scouts were searching for a place to shoot “The Kingdom”, a film about a terrorist attack in Saudi Arabia, they initially chose Dubai. But local officials refused because they were unhappy with the emirate's portrayal in “Syriana”, an earlier film. However, Abu Dhabi, Dubai's sister state within the United Arab Emirates, welcomed the film-makers with open arms. It even provided Apache helicopters for use as props.

Further evidence of Abu Dhabi's determination to turn itself into a centre for media and entertainment came last week when it signed a deal worth $1 billion to woo Hollywood's biggest film studio, Warner Bros, into a partnership. The government has several motives. Abu Dhabi, which claims to sit atop nearly 9% of the world's oil, has boundless wealth. It hopes that spending some of it on media will win it worldwide status and influence in its region.

“In the Middle East you hear a lot about fundamentalists but there isn't a modern media voice that is realistic, dispassionate and factual,” says Riyad al-Mubarak, chief executive of the new Abu Dhabi Media Company (ADMC). “We want to be that voice”. Cynics reckon that Abu Dhabi is also motivated by its rivalry with Dubai, whose relative lack of oil wealth has already prompted it to diversify into tourism, finance and media.

The deal with Warner Bros. requires that each side will spend $500m making big-budget films and video games, to be sold internationally. Profits will be shared equally, but the studio will earn extra cash by distributing the content. It will also earn fees by licensing characters to a new theme park, a hotel and multiplex cinemas, to be built in Abu Dhabi soon. Warner Bros. will make films in Arabic with ADMC too. “These are people with a lot of money and Warner Bros. gives them credibility,” says a film executive.

This month a slate of foreign films will compete in a new festival in Abu Dhabi, just before Dubai holds its fourth such event. The New York Film Academy plans to open a branch in the territory in January 2008 and ADMC is talking to other media-training institutions. Abu Dhabi wants to make its mark in print too: next year ADMC will launch a newspaper in English with about 200 journalists recruited from America, Europe and elsewhere, headed by a former editor of Britain's *Daily Telegraph*. “It's a coming-out party for Abu Dhabi,” says a person involved.

Are the sheikhs wasting their money? The government hopes that ADMC will make a decent financial return at some point. Abu Dhabi can take heart from the international renown of al-Jazeera, a television channel financed by Sheikh Hamad bin Khalifa al-Thani, the emir of nearby Qatar. But it is unlikely that Abu Dhabi would tolerate anything as controversial as al-Jazeera, or risk annoying its neighbours as much as the Qatari channel has done. “We have to be responsible,” says Mr Mubarak. That may hinder Abu Dhabi's ambitions to attract a global audience.

But the initiative may still have impact in the region. Journalists writing in Arabic in Abu Dhabi censor themselves unnecessarily, according to an adviser to the government. The expatriates on the English-language newspaper are less likely to, which may encourage boldness elsewhere. And Abu Dhabi plans to tackle a huge problem for commercial television in the Middle East, which is the lack of a trusted ratings agency to verify viewing figures. ADMC will push for the creation of such an agency for the Middle East—not as exciting as big Hollywood deals, but probably more useful.

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Maltese business

Virtual bridges

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How the euro and technology are changing an island economy

IN THE marinas of Malta there is much talk of gleaming new yachts snapped up by buyers with wads of cash and little interest in sailing. The Maltese lira will disappear in January, when the tiny Mediterranean archipelago joins the euro area. Many Maltese have savings stashed under mattresses and are scared of attracting the taxman's attention if they go to the bank to convert them to euros. Several tax amnesties have yielded little in the way of deposits. Instead, Maltese seem to be rushing to spend their hidden lire on big-ticket items while they still can.

The government is hoping the euro will transport Malta's economy to a bright future based on services. The dwindling of Britain's military presence over the 1970s withered the islands' old fortress economy. With great effort, the authorities lured some manufacturing, including textile factories, microchip plants, and presses that print banknotes. But textiles are drifting off to China and other parts of Asia, and chip foundries might follow, forcing Malta's manufacturers to move upmarket. Increasingly Maltese firms, such as makers of high-quality wooden furniture, are finding that their products are competitive around Europe. Bordeaux's newest posh hotel has doors made in Malta.

Malta is also discovering that in an increasingly virtual world, being an island is no longer an obstacle to providing services, especially in finance and computing. In the late 1980s the government tried building a typical offshore financial-centre, complete with tax sheltering and secrecy. But that got in the way of another Maltese aim—to join the European Union. So the country changed tack and aimed for integration into Europe, with a financial sector that passed all European tests for onshore probity.

One big effect of joining the EU was a surge in inward investment. Last year the flow was around 550m Maltese lire ($188m), more than 25 times the level ten years ago, according to Lawrence Gonzi, the prime minister. Foreigners are attracted chiefly by Malta's tax system, which allows income tax on dividends to be offset against corporate tax, reducing the effective tax rate on dividends from 35% to 5%. It also helps that accommodation and labour costs are between one-half and one-third those of rival hubs, such as Dublin and Luxembourg.

Most of the investment is going into financial services, and one niche in particular: the in-house or “captive” insurance operations of big car-makers. BMW has moved its captive insurance unit from Dublin; Renault, PSA Peugeot Citroën, Volkswagen, Vodafone and RWE have also set up shop in Valletta. These units, which are run by insurance-management firms such as Marsh & McLellan, are allowed to sell a range of other insurance products around the EU. There are also some 250 hedge funds based in Malta. The value of assets under their management has grown sevenfold to €7.5 billion ($10.6 billion) in the three years since EU accession.

Other industries are beginning to follow. Lufthansa, which already services its smaller planes at Malta's airport, plans to tend to its widebody fleet there as well. The Maltese have created a special course for aircraft technicians at a local college to ensure a steady supply of qualified workers. About 20 pharmaceutical firms making generic drugs have also joined the herd of businesses streaming to Valletta, because a wrinkle in Maltese law allows them to do development work on copycat versions of patented drugs and so to be ready to market them in the EU when the patent expires.

But the most spectacular recent arrivals are investors from the United Arab Emirates seeking a European bridgehead. Dubai Holding, an investment firm which has attracted technology giants such as Microsoft, Hewlett-Packard, Cisco and Oracle to a development called Internet City on the outskirts of Dubai, is spending more than $300m to set up a similar facility in Malta. “They wanted a one-stop shop for Europe,” says Mr Gonzi, “and they have undertaken to create 3,500 proper IT jobs.” He is hoping this will attract other big names to Malta. Again, the local vocational college has promised to churn out suitably qualified workers. If only the bigger economies in Europe could move so nimbly in the face of globalisation.

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Face value

The Skype hyper

Oct 4th 2007
From The Economist print edition

Meg Whitman's career at eBay suffers “an impairment write-down”

Reuters

AMONG the many lessons that Margaret (“Meg”) Whitman has picked up during her three decades as a businesswoman, three stand out, she told an audience at Stanford's business school last year. And those three lessons, she implied, explain why she, as boss of eBay, the world's largest online auctioneer, was right to buy an internet-telephone company called Skype for an astonishingly high price in 2005.

The first lesson, which she learned in 1979, was that attention to detail is all important. At the time, she was fresh out of Harvard Business School and just starting her first job at Procter & Gamble. She was charged with figuring out whether the nozzle on shampoo bottles should be half or three-eighths of an inch wide. Despite the tediousness of the task, “I decided I was going to do the very best job that had ever been done at the Procter & Gamble company”, on whose board she now sits. Bring that sort of “execution” to a firm with as much potential as Skype, she suggested, and the sky would be the limit.

The second lesson occurred in 2002. As boss of eBay, she had noticed that a lot of the sellers and buyers on its site were using an online-payment service called PayPal as a sort of virtual wallet, so she decided to buy it. She negotiated for a year, during which the price kept rising. She concluded that in the internet industry one bids early, boldly and pre-emptively high. That is what she did with Skype.

The third lesson was that in such a fast-moving realm “the price of inaction is far greater than the cost of a mistake.” In any case, mistakes can always be corrected. In other words, it did not matter that the “synergies” between a telephone service and an online flea-market seemed few and far between. In her view, eBay was right to buy first and look for the answers to such concerns later.

Collectively, these three lessons have led to disaster. On October 1st eBay conceded, in the language of book-keepers, that the purchase of Skype was just that. It had paid $2.6 billion up front, and agreed to cough up yet more if Skype met certain targets. It did not. This week eBay said that it would take a $1.4 billion charge in relation to the purchase. A portion of the payment is a settlement that absolves eBay of any further obligations to Skype's original owners. But the bigger part, a so-called “impairment write-down”, represents eBay's loss on its ill-fated investment.

Ms Whitman does not even seem to have remembered her own lessons. In terms of the first, eBay's “execution” in integrating Skype with its main business has been poor. Skype's service has deteriorated: it collapsed completely for two days in August. The second lesson—bid early and high—was observed to a fault. As for the third lesson, the mistake has now been admitted, but not fixed.

Ms Whitman should have known better, because Skype became and continues to be a revolutionary technology precisely because it does not extract much revenue from its customers. “We want to make as little money as possible per user,” Niklas Zennstrom, Skype's co-founder, has said. Skype's

breakthrough, in his view, was to point the way towards a time when all voice communication would cost the consumer nothing at all. This week Mr Zennstrom stepped down as Skype's boss; he plans to spend more time on his next disruptive technology, called Joost, which brings television to computer screens.

The rest of Silicon Valley has greeted Ms Whitman's misfortunes with *Schadenfreude*. But the gloating may be short-lived. By buying Skype, the internet phenomenon of 2005, eBay started a bubble. Google, with its purchase of YouTube, the cyber-star of 2006, inflated it further. And Microsoft and Google now appear tempted to add more froth by investing a silly sum in Facebook, the latest big thing. All three—the internet telephone firm, the video site and the social network—make almost no money. EBay's disappointment with Skype is a timely reminder of where this fad might lead.

Down to earth, but with a thud

Until now, Ms Whitman has not faced serious public criticism. The press, *The Economist* included, has churned out many an unquestioning paean to her. In part, that is thanks to her sensible, down-to-earth demeanour, an endearing contrast to the self-aggrandising swagger of other Silicon Valley bosses. Ms Whitman loves to go fly-fishing with her sons; she also enjoys recounting how embarrassed they were when she was voted onto a list of “worst-dressed billionaires”. People want to love her, one analyst argues, which might explain why eBay's shareholders allowed her to throw a desperate “Hail Mary pass” at Skype, in the words of another.

Shareholders at eBay, at any rate, will surely now start asking what on earth Ms Whitman, a seasoned executive, was thinking. Certainly, she felt pressure from Wall Street to come up with a big idea to maintain the firm's breakneck growth. Its main business, brokering auctions, has been slowing. In the year to June, product listings on its site fell for the first time ever, by 6%. Like Yahoo!, its neighbour in Silicon Valley, eBay may be gored by Google, the ubiquitous search engine. Increasingly, people with goods to sell set up their own websites and find buyers by advertising on Google's search pages. Google has also begun offering online payment and telephone services that compete directly with PayPal and with Skype.

Ms Whitman also mentioned a fourth lesson during her talk at Stanford. Her main job as boss, she said, is to put “the right person in the right job at the right time”. She emphasised the word “time”, since a manager who was right a few years ago may no longer be today. It is a lesson her own bosses, on eBay's board, will doutbless soon be reviewing.

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Business and caste in India

With reservations

Oct 4th 2007 | BANGALORE, CHENNAI AND DELHI
From The Economist print edition

Landov

India's government is threatening to make companies hire more low-caste workers

Get article background

A 23-YEAR-OLD dressed in white pyjama trousers and a black over-shirt represents two worlds in India that know almost nothing of each other. One is fast growing, but tiny: the world of business. Strolling through the Californian-style campus in Bangalore that serves as the headquarters of Infosys, a computer-services company, she grins and declares herself glad. Her brother, she adds shyly, is so proud that she is an “Infoscion”.

He is in the rural world where 70% of Indians reside: cultivating the family plot in Bannahalli Hundi, a village near Mysore. Life is less delightful there. Half the 4,000 population are *brahmins*, of the Hindu priestly caste. The rest, including the software engineer and her family, are *dalits*, members of a “scheduled caste” that was once considered untouchable.

Sixty years on this is still the case in Bannahalli Hundi, says the young woman, who does not want to be named. She has never entered the house of a *brahmin* neighbour. When a *dalit* was recently hired to cook at the village school, *brahmins* withdrew their children. Has there been no weakening of caste strictures in her lifetime? “I have not seen it,” she says.

The tale is in startling contrast to Infosys's modernity, and she is embarrassed by it. But it partly explains how she came to be hired by a company that is considered to be one of India's best. She is the beneficiary of a charitable training scheme for *dalit* university-leavers that Infosys launched last year.

In collaboration with the elite Bangalore-based International Institute of Information Technology (IIIT), Infosys is providing special training to low-caste engineering graduates who have failed to get a job in its industry. The training, which lasts seven months, does not promise employment. But of the 89 who completed the first course in May, all but four have found jobs. Infosys hired 17.

The charity was born of a threat. India's Congress-led government has told companies to hire more *dalits* and members of tribal communities. Together these groups represent around a quarter of India's population and half of its poor. Manmohan Singh, the prime minister, has given warning that “strong measures” will be taken if companies do not comply. Many interpret that to mean the government will impose caste-based hiring quotas.

Quotas already apply in education and government, where since 1950 22.5% of university places and government jobs have been “reserved” for *dalits* and tribal people. In addition, since 1993, 27% of government jobs have been reserved for members of the Other Backward Classes (OBCs)—castes only slightly higher up the Hindu hierarchy.

Promoting the wretched

This is not enough for supporters of reservations. Since the introduction of liberal reforms in the early 1990s, public-sector hiring has slowed and businesses have boomed. Extending reservations to companies, they argue, would therefore safeguard an existing policy of promoting the Hindu wretched. It would almost certainly require changes to the constitution. But low-caste politicians are delighted by the prospect, so it could happen.

The chief minister of Uttar Pradesh, a *dalit* leader called Mayawati, has said 30% of company jobs should be reserved for *dalits*, members of the OBCs and high-caste and Muslim poor. Chandra Bhan Prasad, a *dalit* journalist, applauds this and argues that it would be in the interest of companies. “It is in the culture of *dalits* that they are least likely to change their employment because they are so loyal to their masters,” he says. It would also help them become a “new caste [sic] of consumers”.

Businessmen are unconvinced. Government, in both its intrusiveness and its incompetence, is a hindrance to them. Caste-based hiring quotas would be just another burden. People given a right to a job tend not to work very hard. So, in an effort to avert Mr Singh's threat, many companies and organisations that represent them are launching their own affirmative-action schemes.

The Confederation of Indian Industry has introduced a package of *dalit*-friendly measures, including scholarships for bright low-caste students. The Federation of Indian Chambers of Commerce and Industry plans to support entrepreneurs in India's poorest districts. Naukri.com, India's biggest online recruitment service, with over 10m subscribers, anticipates that companies will soon actively seek low-caste recruits. It has therefore started asking job-seekers to register their caste.

Basic training

Infosys's training scheme, as described by S. Sadagopan, the IIIT'S director, is a Pygmalion undertaking. Meeting the parents of his *dalit* students, he saw “almost an anger in their eyes”. For the first month the

students were unresponsive. Their English was dismal. Mr Sadagopan felt compelled to introduce lessons in self-presentation, including table manners.

Matters improved. The course was based on Infosys's 16-week basic training, which 31,000 Indian graduates underwent last year. The low-caste lot scored similar marks and gained confidence. At a bonding session, filled with meditation and dancing, they wrote themselves a slogan: “As good as any, better than many”.

It is a moving story. But Mr Sadagopan's students were not all that deprived. In the words of three, now working for Infosys, they were “normal middle-class Indians”. A third of them were the sons and daughters of professionals. The worst had grades only a little below what Infosys routinely demands of its recruits. Almost all were from urban areas, where caste discrimination is rare.

One of them, Manjunath, says the only time he was ever reminded of his low caste was when he applied for a place at university. Had it not been reserved for him, he says, he might have worked a bit harder—and so joined Infosys without any special help. As for his colleague from Bannahalli Hundi, coming from one of the richer families in the village, she is its first female university graduate—of any caste.

The most that can be said for Infosys's programme—without devaluing Mr Sadagopan's efforts—is that it is a great opportunity for a tiny number of middle-class Indians, who happen also to be low-caste. The same would be true of caste-based reservations. This is because the percentage of India's workforce employed in the “organised” private sector (made up of firms that declare they have ten or more employees), where reservations might be applied, is also tiny: around 2%. And as far as anyone can tell (companies do not ask the caste of their employees), members of low castes are already well represented in low-skilled jobs there. Much of India's heavy industry, such as steelmaking, is located where the low-caste population is high. Tata Steel, which employs around 40,000 people in India, has its main operations in Jamshedpur, in the eastern “tribal belt”.

Membership of a caste, as of a guild or a church, provides businessmen with a useful network. In the informal economy, where banks fear to tread, caste bonds tend to be affirmed through business. The fact that most Indian companies are family-owned exaggerates this: to prevent wealth being diluted, it encourages marriages not only within the same caste, but also within the same family. A sugar baroness of south India's *kamma* caste, Rajshree Pathy, recently explained this practice to an Indian newspaper, the *Business Standard*: “The PSG family produces girls, the Lakshmi Mills family produces boys, they marry each other and live happily ever after.”

The modernisation of India's economy has brought more dynamic change. Among educated, urban Indians caste identity is fading. Inter-caste marriages are increasing. According to Jeevansathi.com, a matchmaking (or, as Indians say, “matrimonial”) website, 58% of its online matches involved inter-caste couples. Meanwhile, in rural India—where unions are not fixed online—intra-caste marriages remain the norm.

Business has to some degree been a laggard in this process. Caste bonds rooted in expediency, not tradition, allow businessmen to borrow and lend money with a degree of accountability, which helps to minimise risk. They are not an affirmation of a vocational hierarchy within the Hindu universe. Nonetheless, in north India, where business is to this day dominated by members of ancient trading castes, like *marwaris* (whose famous names include Birla, Bajaj and Mittal) and *bania* (Ambani), it can look pretty traditional.

Rites of passage

Harish Damodaran investigated the caste origins of many of India's industrialists in a forthcoming book*. He identified three main trends. The first, which he calls a “bazaar to factory” route, is the passage of hereditary traders into industry. In northern India, some castes' monopolies have discouraged them from leaving their traditionally prescribed employment. So members of north India's farming castes—for example, *jats* and *yadavs*—rarely own a sugar or flour mill.

The second trend, “office to factory”, describes a recent movement of well-educated high-caste Hindus, including *brahmins*, into business. Lacking capital, these sophisticates tended to enter the services sector, where start-up costs are relatively low. India's world-class computer-services industry, including companies like Infosys, is the result.

The third trajectory, “field to factory”, is the transition into the business world of members of India's middle and lower-peasant castes. This must be the path of India's *dalits*, too. But they have not trodden it yet: across India, Mr Damodaran could not find a significant *dalit* industrialist.

There is no strong evidence that companies discriminate against low-caste job applicants. Upper-class Indians, who tend also to be high-caste Hindus, can be disparaging about their low-caste compatriots. “Once a thicky, always a thicky,” is how a rich businessman describes Ms Mayawati. Yet this at least partly reflects the fact that low-caste Hindus tend also to be low class; and in India, as in many countries, class prejudice is profound.

There is, on the other hand, plenty of evidence that few able low-caste graduates are emerging from India's universities. Since it began registering the caste of its subscribers—almost by definition computer-literate and English-speaking—Naukri.com has added 38,000 young *dalit* and tribal job-seekers to its books. That represents 1% of the total who have registered in that time.

For reservationists, this confirms the need for quotas. Others interpret the facts differently: reservations don't seem to work. And statistics support this view. Reservations notwithstanding, low-caste Indians are getting less poor at almost the same rate as the general population. Between 1983 and 2004, their spending power increased by 26.7%, compared with 27.7% for the average Indian, according to the National Sample Survey Organisation, a government body.

Low-caste students struggle in schools without special help, which is rarely available. Their English—the language of India's middle class—tends to be poor. Many drop out. Up to half of university places reserved for low-caste students are left vacant. So, too, are many of the university posts reserved for low-caste teachers. Most Indians emerge from this system with an abysmal education. Low-caste Indians perhaps almost invariably do.

A measure of this fiasco can be found at the political-science department of one of India's prestigious post-graduate universities. Each year it chooses 50 students, from 1,500 applications, for its master's degree. Successful applicants will average no less than 55% in their undergraduate exams. *Dalit* applicants scrape in with as little as 30%. Nonetheless, practically every student will be awarded a first-class degree.

India is failing to equip its young, of whatever caste or religion, with the skills that its companies need. This is one of the biggest threats to sustaining high economic growth. India's outstanding computer-services companies—which will account for around a quarter of overall growth in the next few years—intend to hire over 1m engineering graduates in the next two years. It will be tough. To recruit 31,000 graduates last year, Infosys considered 1.3m applicants; only 65,000 passed a basic test. To address the skills shortage, the company is investing a whopping $450m in training. “We are building India's human resources,” says Mohandas Pai, Infosys's chief of human resources.

Alas, reservationists have other concerns. Caste politics are pervasive. On August 28th the Supreme Court struck down an effort by Andhra Pradesh's government to reserve 4% of government jobs and education places for poor Muslims. The court is meanwhile weighing a more dramatic measure announced by the government last year: to reserve 27% of university places for the OBCs. To placate irate students, many of them high-caste, the government promises to increase the number of university places accordingly. Education standards would no doubt fall further.

Even so, the policy may be unstoppable. Since reservations for the OBCs were introduced in the early 1990s the rise of political parties dedicated to these groups has been inexorable. So has the proliferation of the OBCs, to around 3,000 castes. They include millions who are not poor at all.

“A massive deliberate confusion” is how Surjit Bhalla, an economist at Oxus Investments, a hedge fund, characterises reservations for the OBCs. When they were awarded reservations, the OBCs were estimated to make up 53% of India's total population. More recent counting suggests they are only about one-third of the population, although their 27% reservation remains unchanged. Moreover, by most measures, the average OBC member is no poorer than the average Indian. “How can you discriminate against the average?” asks Mr Bhalla, despairingly.

There by mistake

And despair he may. Practically no politician dares speak out against this caste-based racket for fear of

being labelled an apologist for the caste system. Rather like guests at the Hotel California, those that join the list never leave—even one or two castes that were allegedly included by mistake. The surpassing example is Tamil Nadu, which reserves a total of 69% of government jobs: 1% for tribal people, 18% for *dalits*, 30% for the OBCs and 20% for a subset of them—members of castes once categorised by British colonisers as “criminal tribes” and now known more delicately as “de-notified communities”.

There is little opposition to this policy in Tamil Nadu, for two reasons. It is one of India's more literate and prosperous states. And low-caste Hindus are unusually prominent in Tamil Nadu, which suggests to reservationists that the policy is working well. Textiles companies in Tirupur, a T-shirt hub, for example, are mostly owned by *gounders*, members of a peasant caste that is officially listed as an OBC.

One defender of the policy is N. Vasudevan, chief official of the Kafkaesque vision of bureaucratic hell that is the Backward Classes, Most Backward Classes and Minorities Welfare Department in Chennai, where workers languish behind mountains of never-opened files. Asked when it might end he replies: “When everyone becomes equal.”

There is an alternative view: that Tamil Nadu is more equal than most states not because it has lots of reservations but because, overall, it has been run less badly. It has therefore delivered above-average economic growth, from which low-caste Tamils have benefited.

In addition, low-caste businessmen in Tamil Nadu have had opportunities that have nothing to do with government policy. In contrast to north India, where commerce is dominated by members of a few business castes, south India's business community has been more open to members of non-business castes. According to Raman Mahadevan, a business historian, this is partly because members of the south's main trading caste, the *chettiars*, chose to concentrate their investments outside India during the 19th century, in Malaya and Singapore.

Partly as a result, little large-scale industry emerged in southern India until the 1930s. Around the same time, a popular movement against *brahmins*—especially lordly in the south—emboldened members of the lower and middle castes, including *gounders*, who were quick to convert their new assertiveness into business.

The Hindu caste system has never been rigid. Low-caste Hindus do not accept their lumpen position in the hierarchy. Indeed, like middle-class English families, they tend to cherish a myth of their former greatness. By imitating the habits of a more prestigious neighbour, in dress or ritual, some low castes have sneaked a rung or two up the ladder. More recently, in an effort to be classified as an OBC or a *dalit* caste, some middle-ranking castes have tried to climb a rung or two down.

Meanwhile, on the lowest rung of the ladder, *dalit* businessmen can be found operating in the informal economy, perhaps as small traders. They must be especially reliant on caste as a business network. But that reliance will change if they can expand into the organised sector. Where businessmen can gain access to credit without having to claim kinship, caste affiliations wither. As Mr Damodaran writes: “A *kamma* sugar magnate ultimately identifies his interests with other mill-owners and not with fellow *kamma* cane growers or workers.” And his business may flourish, unfettered.

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* “India's New Capitalists: Caste, Business and Industry in a Modern Nation-State.” By Harish Damodaran. Permanent Black/Palgrave Macmillan.

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Stockmarkets

Bad-news bulls

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Reuters

Stockmarkets are breaking records again as if the credit crisis were ancient history. If only it were

THE news seems to go from bad to worse. In late September figures showed that the American housing market was in free fall, with both sales and prices plunging. On October 1st Citigroup and UBS, two of the world's biggest banks, said they were writing down $9.3 billion of debt between them because of the credit crunch.

Global stockmarkets have reacted not with dismay but with euphoria. Wall Street marked the Citigroup write-downs by driving the Dow Jones Industrial Average to a record high (see chart). The MSCI emerging-markets index has soared to new highs. This summer's turmoil seems to have been completely forgotten.

What explains this apparent insouciance? It seems that investors reckon they cannot lose. “Take your pick,” says Gerard Minack, a strategist at Morgan Stanley: “Equity markets are either behaving as if the worst is over for credit and housing problems or they remain convinced that the [Federal Reserve] can offset whatever bad news may unfold.” In other words, bad economic news means the Fed will cut interest rates and good news means recession will be avoided.

There are some signs to support the idea that the worst might be over in the credit markets. After strenuous effort, banks have managed to find buyers for $9.4 billion of the $24 billion needed to finance the takeover of First Data, a payments processor, by Kohlberg Kravis Roberts, a private-equity firm. According to JPMorgan, even the structured products that caused so much disquiet during the summer are moving again—$6.2 billion of collateralised-debt obligations were issued in the last week of September.

Risk appetite is resurfacing in currency markets, too. The “carry trade”, the borrowing of low-yielding currencies to buy higher-yielders, is back in full swing; the Australian and New Zealand dollars have been surging. Having reached a 27-year high on October 1st, gold (often seen as a safe haven for nervous investors) suddenly lost 2.5% of its value in a day.

The bullish case seems fairly simple. The American economy may be slowing but the rest of the world,

particularly emerging markets, can make up for it. As a result, corporate profits can continue to be strong. Profits forecasts are being revised down, but not dramatically so. Ian Scott, a strategist at Lehman Brothers, says that in America there have been just 71 profit warnings after the third quarter, compared with 114 warnings at the same stage in 2005 and 173 in 2004. The dollar's decline has added impetus to the earnings of American exporters and multinationals with overseas subsidiaries.

In this light, the credit crunch seems like old news. Even bank write-downs can be spun in a good light. Much of the panic in August was caused by fear of what banks had on their books; now the bad news is out, investors can relax.

In addition, many investors are looking back to 1998 when the Fed cut rates in response to a previous crisis in the finance industry—the collapse of Long-Term Capital Management, a hedge fund. The markets recovered quickly and the dotcom bubble reached its apogee. This time round, emerging markets (or even alternative energy stocks) might be the big winners. And in the short term at least, money that was pouring into the credit markets is now being invested in shares.

But not everyone buys the bulls' arguments. Experienced observers of the debt market, such as Tom Jasper of Primus Guaranty, a credit insurer, think the crunch is far from over. According to Moody's, a rating agency, the spread (excess interest rate) of high-yield debt over Treasury bonds has fallen from the crisis peak but is far higher than it was in June.

In the quick-to-rollover money markets, there is still a much wider spread than normal between the rate governments must pay to borrow money and the rate which big banks have to pay. That indicates investors remain nervous about the extent to which banks are exposed to losses from subprime mortgages, or large private-equity borrowers.

Problems in the housing markets are far from over, too. The latest gloomy statistic to emerge was a 21.5% annual fall in pending American home sales, a figure that is a leading indicator for actual sales. House prices will surely fall further and defaults increase, as homeowners struggle to cope with higher mortgage rates from “teaser” loans taken out in 2006.

That may well have a depressing effect on consumer sentiment, something which the Fed's rate cut last month may do little to help. Normally, interest-rate moves take 12-18 months to work their way through the economy. In any case, mortgage rates are barely lower than they were a month ago. The American economy could yet slip into recession, an event on which Goldman Sachs now places a 40% probability.

Even the argument that corporate profits are still strong does not look completely convincing. American profits are close to a 40-year high relative to national output, according to Longview Economics, a financial consultancy. That suggests they should return to the mean, especially as the profit numbers taken from national-accounts data look a lot weaker than those reported by quoted companies. The last time such a gap appeared was in the late 1990s, an era of much creative accounting.

And while the weak dollar may be good news for American exporters, it is bad for European companies. Having been strong in the early part of this year, the latest data on European economies have weakened sharply; Nicolas Sarkozy, the French president, is not the only one concerned by the euro's strength. There is the potential for turmoil in the currency markets, either because Europe takes a stand against the rising euro at the Group of Seven finance ministers' meeting on October 19th, or because international investors, who have to finance the American trade deficit, become alarmed by the weakness of the dollar. Stockmarkets might be able to rise above the problems of the credit markets. But whether they could gain ground in the face of foreign-exchange market turmoil as well seems a lot more doubtful.

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China's stockmarkets

Rush hour

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Share prices in China have taken on a life of their own

Get article background

TRAFFIC jams were not only to be found on the streets of Hong Kong this week. Share-trading systems were also clogged up as investors piled in after a holiday to mark the founding of the People's Republic of China. Mainland markets were closed for the Golden Week, which only seemed to drive more money to Hong Kong. On October 2nd the Hang Seng index closed above 28,000 for the first time, rising 3.9% in one day. Shares of mainland Chinese firms climbed even higher amid talk of heavy buying by institutions in China able to invest in Hong Kong.

A day later prices eased, but the gossip didn't. There were rumours that the Hong Kong stockmarket would attract some of the new $200 billion sovereign-wealth fund created by China's government. An announcement in August that ordinary Chinese would be allowed to invest in Hong Kong has also raised hopes of still more money to come. In China, most industries are caught up in the excitement, but in Hong Kong, shares of mainland firms trade at a discount to those in their home markets. That means arbitrage opportunities abound.

The bull market should make life sweet for securities analysts—at times, too sweet. Citigroup, for example, put a strong buy recommendation on China Resources Land, a property company, in mid-September, saying the share price could appreciate by 20%. Two weeks later, it had. Next big idea?

What if there are none? Certainly at some point rational price-earning assumptions will suggest there is nothing left to buy. Shares on the Chinese bourses have jumped to almost 65 times historic earnings from the 50s a week ago (see chart). Yet there is something suspiciously circular about the valuations because many firms profit from investing in shares. Future expectations, meanwhile, are staggering. The Hong Kong stock exchange trades at 39 times book. The ten-year average is six times.

Even the Chinese government is worried. To cool the markets down, it has imposed transaction taxes and higher interest rates. The management of the Shenzhen Stock Exchange has tried to talk the market down—to no avail. Officials should instead promote better disclosure so that investors can find out what they are buying. Transparency, however, is sensitive in China. Some assume that the Chinese government has too much at stake to let the market fail: the upcoming party congress, for example, or stable conditions ahead of the 2008 Olympics. Foreigners appear to buy that argument. Flow-of-funds data from Citigroup show that they continue to pour money in. Perhaps they think it is crazy to miss out on the madness.

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Banking

As bad as it gets?

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Banks on both sides of the Atlantic announce poor results

AFTER the summer's horrors, investors in banks needed something on which to hang their hopes. That something was the kitchen sink. On October 1st UBS, Credit Suisse and Citigroup all gave warning that earnings would be hit in their third-quarter results and all saw their share prices rally afterwards. Deutsche Bank got a similar response on October 3rd, after it said that it would take a charge of €2.2 billion ($3.1 billion) on its fixed-income activities. Investors appear to be betting that the banks have thrown everything bad into their assessments—a tactic known in the trade as “kitchen sinking”—paving the way for better times ahead. They may yet be disappointed.

UBS had the nastiest surprise to impart. The Swiss bank expects to report a loss of between $515m and $690m in the third quarter, thanks largely to a $3.4 billion write-down on its fixed-income assets, many of them securities backed by American subprime mortgages. UBS is the first heavyweight bank to go into the red as a result of the summer's financial turmoil (although differences in earnings calendars play some part in that). Given its relatively small fixed-income business, the scale of UBS's exposure to subprime mortgages indicates some serious flaws in what had once been thought of as a relatively conservative risk-management apparatus. The announcement by Credit Suisse, a perennial rival, that it still expected to make a profit this quarter compounded the embarrassment felt by UBS.

The response was swift. Marcel Rohner, UBS's chief executive, announced 1,500 job losses, turfed out some senior managers and appointed himself head of the investment-banking division. The bank now intends to play to its strengths in areas such as equities and advisory work. That makes sense. The real value of an investment bank to UBS, and Credit Suisse too, lies in services that overlap with its thriving wealth-management arm, not in making big bets on American mortgages. Mr Rohner can also claim that the mess was not of his making: he was installed in the top job only in July after the failure of Dillon Read Capital Management, an in-house hedge fund.

Chuck Prince, the boss of Citigroup, has much more egg on his face after saying that the American bank's profits for the quarter would plummet by 60% compared with the same period of 2006. Mr Prince's ill-timed comment in July that Citigroup was still dancing to the music of the buy-out boom is being replayed endlessly now that things have ended in such discord. Citigroup announced write-downs of $1.4 billion on commitments to leveraged buy-outs, as well as further substantial losses on mortgage-backed securities and fixed-income trading. Unlike UBS, Citigroup expects to have remained easily in profit during its third quarter but Mr Prince, whose four-year tenure has been dogged by criticism, is under severe pressure.

Expectations are high of hefty write-downs at banks that have yet to report. On October 3rd Merrill Lynch sacked the head of fixed-income trading, which is also assumed to have done badly. The big question is whether a line is really being drawn under the turmoil. Banks have every incentive to be conservative when investors are braced for the worst: UBS is taking big losses on highly rated debt as well as its subprime securities. There are also signs of recovery in the credit markets. Mr Prince, tempting fate again, predicted a return to “a more normal earnings environment”.

But the assumptions behind some of the banks' write-downs remain murky, and there are worrying indications of more economic weakness. A big part of Citigroup's decline in earnings came from its consumer business, where rising defaults and higher loan-loss reserves, bumped up on signs that customers may be having more trouble keeping up with payments, chewed up a whopping $2.6 billion. These might not be the write-downs to end all write-downs.

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Buttonwood

To infinity and beyond

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Contrary to popular belief, stocks do not always go up

IF AMERICAN investors have learned any lesson in the last 25 years, it is to buy shares on the dips. The slide in 2000-02 may have been longer and deeper than they were used to but normal service was eventually resumed, driving the Dow Jones Industrial Average to a record high on October 1st.

Among American financial commentators, it is almost universally accepted that shares always rise over the long run. And this perception does seem to be backed up by evidence; if you take any 20-year period, Wall Street has always delivered positive real returns. In addition, one ought to expect shares (which are risky) to deliver a higher return than risk-free assets such as government bonds.

Nevertheless, investors ought also to remember the world's second largest economy, Japan. Its most popular stockmarket average, the Nikkei 225, peaked at 38,915 on the last trading day of the 1980s; this week, nearly 18 years later, it was still only around 17,000, less than half its peak. Buying on the dips did not work either. By 1994, the Nikkei had fallen to 21,000—at which point a technical analyst, after poring over his charts, told this columnist that it had to be one of the great long-term buying opportunities.

Investors who suffered through the Depression, when American stocks fell almost 90% from their peak, at least had a decent dividend yield to hold on to. But the Japanese market has offered a paltry yield throughout this period.

Japan might seem to be an exception. Arguably, America is just as much of a special case. Think back to the start of the 20th century when investors might have picked Russia, China and Germany as the rising stars of the next 100 years. Within the next half-century, investors in the first two saw their holdings wiped out by revolution while world wars and hyperinflation ruined the portfolios of those who backed Kaiser Wilhelm II's empire.

Elroy Dimson, Paul Marsh and Mike Staunton of the London Business School examined* the record of 16 stockmarkets which were in continuous operation over the course of the 20th century. In itself, this selection showed survivorship bias by excluding the likes of Russia and China. The academics found that only three other countries could match the American record of having no 20-year periods with negative real returns.

Other investors were far less lucky. Japanese, French, German and Spanish investors all suffered instances where they had to wait 50-60 years to earn a positive real return; in Italy and Belgium, the waiting period stretched to 70 years. It was no good following the famous advice to “put the shares in a drawer and forget about them”; the furniture would not have lasted that long.

Besides survivorship bias, there is another problem with the belief that stockmarkets must always go up; the very existence of the belief is likely to lead to its falsification. Investors will keep buying until prices reach stratospheric levels. That clearly happened in Japan in the late 1980s and with the technology-heavy NASDAQ index in the late 1990s; the latter is still, after seven years, not much more than half its peak level.

A significant proportion of the return from equities in the second half of the 20th century came from a re-rating of shares; investors were willing to pay a higher multiple for profits. But re-rating cannot continue forever. Although ratings have fallen significantly since the heady days of 2000, that is in large part due to the remarkable strength of corporate profits, now close to a 40-year high relative to national output. If profits revert to the mean, that could act as a drag on stockmarket performance. And, as with Japan, investors do not have much in the way of income to fall back on; the dividend yield on the American market is just 1.7%.

If investors want a simple parallel with share prices, they need only turn to the American housing market.

Back in 2005, Ben Bernanke, then an economic adviser to the president, was asked about the possibility of a decline in house prices on CNBC, a financial-television channel. He said, “We've never had a decline in housing prices on a nationwide basis. What I think is more likely is that house prices will slow, maybe stabilise.”

Lots of people took the same view and were willing to borrow (and lend) on a vast scale on the grounds that higher house prices would always bail them out. They are now counting their losses. Investors in equities should beware of overcommitting themselves on the basis of a similar belief. Just ask the Japanese.

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* “Irrational Optimism”. *Financial Analysts Journal*, January/February 2004

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Remittances to Latin America

Counting the cash

Oct 4th 2007 | MEXICO CITY AND WASHINGTON, DC
From The Economist print edition

Less money is being sent home by migrants. That is not as bad as it sounds

IT IS testament to the love of fathers for sons, of children for parents, of husbands for wives. In the past five years, Mexican immigrants to America, most of them in back-breaking jobs on farms and building sites, sent more than $90 billion home to their families. That's $900 for every man, woman and child in Mexico, or two thirds of a year's salary on the minimum wage. In recent years the flow of remittances has grown fast, averaging 22% annually in 2001-06. Growth rates in Central America have been even higher.

This remarkable period of growth now seems to be drawing towards a close: Mexico's central bank estimates that between January and July this year remittances were only 1.6% greater than in the same period of 2006. According to Jesus Cervantes, an economist at the central bank, in seven of Mexico's 32 states the amount actually declined.

Plenty of reasons have been offered to explain the slowdown, not all of them wholly convincing. Some blame America's slowing housing market; according to the Pew Hispanic Centre, a research institute, almost a fifth of construction workers in the United States are foreign-born Hispanics. However, Jorge Sicilia, an economist at BBVA Bancomer, a Mexican bank, notes that because the Hispanic labour market in America is so flexible, workers can probably find jobs in places other than building sites.

Others argue that tightened enforcement of immigration laws has affected how much money migrants send home. Salo Eduardo Levy, a director of Western Union, a money-transfer firm, told a recent conference in Washington, DC, that some people call to ask if there are immigration authorities nearby before sending payments. Western Union, he said, has never seen its customers so nervous.

All of these may be plausible explanations. But the main reason for the slowdown is more prosaic: economists have become better at tracking the flow of remittances, because more of them than ever before are sent through easily traceable channels.

In 1995 money orders sent by post accounted for 40% of remittances, says Mr Cervantes. Last year, they were just 4.5% of the total. The sending of cash has also declined. Instead, almost all the money heading south now does so electronically and so can be traced more easily. The heady growth rates of recent years were an exaggeration—mostly explained by the fact that more money was being counted. Now that the switchover has happened, growth rates are almost bound to decline.

This is good news for Mexico and Central America. Remittances in Mexico are the second-largest source of foreign income, after oil, and ahead of tourism. In some states, such as the central state of Michoacán, they amount to as much as 12% of the economy.

But they are only 3% of Mexico's GDP, and a slight change is unlikely to have a big impact on the exchange rate, inflation or economic growth. For ordinary Mexicans, who need the cash so badly, the absolute level is anyway far more important.

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Pandemic planning

Flu fighters

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From The Economist print edition

The finance industry is keeping an eye out for the next crisis

DOES this sound familiar? A crisis lasts for weeks, is driven by uncertainty over who is suffering and has people queuing to withdraw cash. The credit crunch may have preoccupied the banking world this summer but the risk of something much worse lurks: an avian flu pandemic, perhaps. In America the largest-ever exercise to simulate the impact of that sort of pandemic on the industry is under way. Over three weeks ending on October 12th, 2,725 financial institutions are being fed scenarios on the spread of a virtual outbreak as well as a weekly batch of letters of the alphabet. Banks must assume that employees whose surnames start with those letters are unable to work, a simple but effective way of aping the indiscriminate nature of a pandemic.

The American simulation is closely modelled on a similar exercise carried out by the Financial Services Authority (FSA), Britain's financial regulator, in late 2006. One outcome of the British experiment was to force institutions to think much more systematically about human-resource policies. Some had planned to hold stocks of flu medicines but had not designated which employees would be treated. As absentee rates climbed, firms realised that they would need policies on everything from whether staff could take holidays to whether they could attend funerals of dead colleagues. The exercise was “a wake-up call to HR departments”, says Richard Maddison of the FSA.

Retail institutions came under greater strain than wholesale ones because their work is less automated, they have more customer contact and their employees are more likely to be affected by school closures. Since the exercise, British retail banks have been thrashing out ways of co-ordinating branch and cash-machine closures so that bank services remain as widely available as possible. They have also been honing plans for training and redeploying staff from functions such as sales and product development to positions directly serving customers.

As for the risk of a “dash for cash”, Chris Keeling, a business-continuity specialist, reckons that there may be an initial spurt of withdrawals but that it will not last long. There will not be much to spend money on and no one will want to stand in queues. If fears of initial panic may be overdone, the FSA exercise also suggested that the after-effects of the pandemic would be more testing than anticipated. Markets will recover much more quickly than bereaved employees.

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Economics focus

When to bail out

Oct 4th 2007
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The case for more regulation of banks' liquidity

Illustration by Jac

EVEN the fiercest free-market advocates would concede that governments can justly intervene to curtail businesses that become too powerful. Most would allow that dominant firms with the clout to gouge their customers should be broken up or subjected to strict price regulations. Similarly a judicious regulator should penalise polluters for imposing costs on others by taxing their activities. When markets provide the wrong incentives, because there are too few competing firms (ie, a monopoly), or no market price (ie, pollution) or for some other reason, there is a case for the state to act.

But not all regulated firms are monopolists or polluters. Commercial banks are an unusual mix of hazardous might and fragility. Long before he became the Federal Reserve's chairman, Ben Bernanke wrote an influential research paper showing how bank failures in America were largely responsible for the depth and longevity of the Great Depression. Today, even with larger capital markets, banks are still central to the economy's fortunes, as providers of credit and processors of payments.

Yet for all their might banks are fragile entities. What a bank owes in deposits can be quickly called in, but what it is owed in loans to businesses and households cannot easily be converted to cash. This mismatch between liquid debt and illiquid assets makes banks susceptible to sudden losses of funding.

It is partly this vulnerability that makes them candidates for supervision. In a panic, individual depositors have an incentive to withdraw their cash, even if collectively they (and the bank) might be better off if they held fast. This weakness begs for a regulatory hand to co-ordinate actions in the common interest.

There is a second and related fault-line. Banks are less than perfect in the role of providers of ready cash. Demand for liquidity is unpredictable and, for banks, holding liquid assets means forgoing more profitable investments. If there is a sudden rush for cash, banks may prove unable to supply it at an affordable price even to creditworthy enterprises.

These two shortcomings—the co-ordination difficulties that cause bank runs and the problem of sporadic cash shortages—are market failures that have spawned familiar regulatory remedies: deposit insurance and liquidity support. Deposit insurance is a standard antidote to bank runs and is typically financed by a levy on deposit-takers. Coverage has to be large and repayment swift, to deter panic withdrawals. If depositors believe that it will be hard to get their cash tomorrow, they will queue at the counter today—as the throngs outside branches of Northern Rock, a British mortgage lender, recently demonstrated.

The deposit-insurance remedy begets problems of its own. Once depositors are sure of getting their money back, whatever the circumstances, they have little incentive to monitor a bank's business. This weakens the market discipline of *caveat emptor*. But a bank's prospects are so difficult to assess for small depositors that some form of supervision might be necessary anyway.

A more fundamental problem is how deposit insurance distorts banks' incentives. A secure deposit base encourages banks to take excessive lending risks, since the profits go to shareholders and the risks are borne by insurers. One way of mitigating this problem is to charge insurance premiums that vary according to the riskiness of each bank's lending. The more common remedy is to put limits on banks' assets by forcing them to increase their capital if they make risky loans.

The other main plank of state intervention is the liquidity backstop provided by central banks. The regular operations in money markets by the Federal Reserve and its brethren are designed to meet the vagaries of demand for ready cash.

Banks and government have a regulatory pact. In exchange for the stability provided by deposit insurance and the central bank, banks submit to regulatory oversight. The main thrust of regulation is to keep banks solvent by ensuring that their capital is sufficient to cover expected losses.

Solvency or liquidity?

This is fine, up to a point. But recent events suggest that it may not be enough to base a regime solely on capital adequacy. The turmoil in money markets revealed that some banks put aside too few liquid assets to meet a cash squeeze. Many were happy to extend contingent credit lines, apparently secure in the belief that central banks would provide extra liquidity if needed. The private cost to banks of being light on liquid assets was clearly too low compared with the public cost that the liquidity squeeze produced in terms of instability and high interest rates.

For that reason, central banks had little choice but to intervene. Trying to discipline banks after the fact by withholding liquidity risked damaging the economy. But it is galling that the profitability of the banks was partly founded on an excessive reliance on central banks as liquidity providers.

What is particularly worrying is that huge convulsions in money markets were caused by potential losses in subprime lending that are small relative to banks' capital. Unless banks are forced to protect themselves, much bigger shocks in the future might require even larger interventions by central banks. Banking regulation may need to put as much emphasis on banks' liquidity as their solvency. The Basel 2 agreement fine-tunes the risk-capital framework but, as regulators freely admit, it has little to say about provisioning for funding shortages.

Raghuram Rajan, of the University of Chicago's business school (and a former chief economist of the IMF), believes that what is needed is consistent monitoring of banks' liquidity position over the economic cycle. One benefit of the recent crisis, he says, is that it will provide a benchmark for assessing whether banks have enough liquidity in the future. More scrutiny may be the only way to ensure less reliance on the state.

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Evolution

Patience, fairness and the human condition

Oct 4th 2007
From The Economist print edition

Apes are patient, but only people are fair. That may help explain why people came out on top

AFP

PEOPLE love to catalogue the traits they think characteristic of their species. Some, such as language, are obvious. Others, such as patience and a sense of fairness, are more subtle. These traits, however, did not spring into existence fully formed. They evolved—and to understand human evolution it would help to know their genetic underpinnings and the order in which they evolved.

One way of looking at these questions is to compare people with their closest relatives, great apes such as chimpanzees. Another is to compare them with each other. Three studies published this week, which take one or other of these approaches, have cast light on the evolution of both patience and fairness. It turns out that patience is older than fairness. It also turns out that although the propensity to be fair varies a good deal from one person to the next, that variation is rooted in genetics rather than culture.

The origin of virtues

The essence of patience is the ability to delay the gratification of an appetite in favour of a greater ultimate reward. Past tests of the degree to which animals other than people can delay their gratification have focused on birds and monkeys. Both groups can delay gratification if a bigger reward is on offer, but only for a few seconds.

Birds, however, are remotely related to humans, and even monkeys are not as close as apes. In *Current Biology*, Marc Hauser of Harvard University and his colleagues compare chimpanzees and humans directly. Both, it turns out, can be patient to a high degree. In fact chimps are more patient than people.

The human participants in Dr Hauser's experiment were allowed to choose a preferred food, such as raisins or chocolate. The chimpanzees were simply offered grapes—which they usually like. Otherwise the experimental conditions were identical. The choice was between one unit of goodies immediately and three after two minutes. Chimpanzees were nearly four times more likely to wait for the big reward than humans were. This suggests not only that the trait of patience predates the split between humans and chimpanzees, some 4m years ago, but that the trait seems more characteristic of chimps than people.

When it comes to fairness, though, it is a different story. Economic theory has contrived a species it calls *Homo economicus*—a “rational maximiser” who grabs what he can for himself. But, curiously, he makes no appearance in the ultimatum game, a classic economics experiment.

In this game, two players, a proposer and a responder, divide a reward. It could be a cake. It could be cash. It could even be a bunch of grapes. The game is so named because the proposition is an ultimatum.

The responder can either accept the division or reject it. If he rejects it, both players receive nothing.

Homo economicus would accept any division in which his share was not zero. But that is not what happens. Scores of studies have run the ultimatum game across cultures and ages. Universally, people reject any share lower than 20%—apparently to punish the greed of the proposer. People do not act like *Homo economicus*. Instead, they are the arbiters of fairness.

To find out if chimpanzees share this sense of fairness, Keith Jensen and his colleagues at the Max Planck Institute for Evolutionary Anthropology, in Leipzig, designed a way for chimps to play the ultimatum game. Their version started with a pair of trays far from the players' cages. Each tray had ten raisins divided in different ways between two pots—say eight and two, or five and five. One chimp was allotted the role of proposer. He could choose one of the trays, pulling it by way of a rope just halfway to the cage. The other, the responder, could then choose to pull on a rod, bringing the tray close enough for both to get the raisins, one pot for each. If the responder chose not to pull the tray closer within a minute, the offer was considered rejected, and the game concluded.

The result, which Dr Jensen reports in *Science*, is that chimps are simply rational maximisers—*Pan economicus*, if you like. Though proposers consistently chose the highest possible number of raisins for themselves, responders rarely rejected even the stingiest offers.

This is a telling outcome. A number of researchers in the field of human evolution think that a sense of fairness—and a willingness to punish the unfair even at some cost to oneself—is humanity's “killer app”. It is what allows large social groups to form. Without it, free-riders would ruin such groups, because playing fair would cease to have any value. Dr Jensen's previous experiments have shown that chimpanzees are willing to punish actual thieves. But his new data add weight to the theory that the more sophisticated idea of fair shares, which underpins collaborative behaviour, appeared in the hominid line only after the ancestors of the two species split from one another.

Nor, according to the third of this convenient trilogy of papers, is a sense of fairness rooted in culture. Rather, it is genetic—as it would have to be in order to evolve. Paradoxically, discovering this relies on the fact that not everyone possesses it to the same degree.

As they write in the *Proceedings of the National Academy of Sciences*, Bjorn Wallace of the Stockholm School of Economics and his colleagues have shown this by playing the ultimatum game with twins. They used the classic trick of neutralising the effect of upbringing and exposing that of genetics by comparing identical twins (who share all their genes) with fraternal twins (who share half).

Each twin of a pair played the ultimatum game, both as proposer and as responder. Dr Wallace found, in the case of identical twins, a striking correlation between the average division that each member of a pair proposed and also between what they were willing to accept. In other words, their senses of what was fair were similar. No such correlations were seen in the behaviour of fraternal twins.

Besides showing that a sense of fairness has a genetic basis, this result also raises a question: why should the sense of what is fair be so variable? It may be that in a population of the fair, the unfair prosper while amongst the unfair, the fair are better off. The result would be an equilibrium in which various attitudes to fairness do just as well as each other. But why, exactly, that should be the case is a subject for another day's research project.

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Organ transplants

Subprime cuts

Oct 4th 2007
From The Economist print edition

American transplant surgeons need to become less fussy about their kidneys

“RIGHT now, we have two kidneys coming in from Montana; they are 24 hours old and nobody wants them. But they are perfectly good kidneys even though they are going to be 40 hours old before we transplant them.” Thus spoke Robert Stratta, a transplant surgeon and researcher at Wake Forest University Baptist Medical Centre, in North Carolina, on October 1st. Many surgeons in America are reluctant to transplant kidneys that have been out of their original body for that long. They are also unwilling to use kidneys from elderly donors, and are sniffy about those whose function is less than perfect. Dr Stratta thinks differently—and if all has gone well, by the time this article was printed on October 4th two people will have received potentially life-saving organs that might otherwise have been thrown away.

For the 73,458 Americans waiting for a new kidney, it matters that every donated organ is put to good use. At the moment, there are only about 17,000 transplants a year there. Yet, according to Dr Stratta, up to two-thirds of donated kidneys are rejected as sub-standard. That compares, for example, with a rejection rate of 3-4% in Britain. He and his colleagues think many of the rejects are perfectly serviceable—and they act on their belief.

That belief, though, is backed up by data. In one of the studies carried out at Wake Forest, which was presented this week at a meeting in Prague of the European Society for Organ Transplantation, Dr Stratta and his colleagues compared the outcomes of transplants of organs that matched the standard acceptance criteria with those for “extreme” organs of the sort most American surgeons reject.

Such organs include kidneys from donors aged over 70, from donors whose hearts had stopped beating and thus deprived the organ in question of oxygen (as opposed to those who had suffered brain death in which their hearts kept beating), and even organs in which more than 30% of the filtering units were not working. The researchers found that after 30 months the two groups had experienced similar clinical outcomes. The extreme kidneys, in other words, had performed as well as those in the pink of health.

As it turned out, the most important reason for the failure of a transplant was neither the quality of the kidney nor the history of the donor, but the delay between its removal and its re-insertion. Kidneys do not like to be idle. They wither when they are not filtering blood and producing urine. Dr Stratta says that this loss of function can be reduced considerably by using pumps to force a suitable fluid through a kidney to keep it busy. Death rates can also be lowered by matching the age of the recipient with that of the donor. This is because the demands on a kidney vary with age. Younger patients need younger kidneys.

Of course, 30 months is not a lifetime, and Dr Stratta concedes that extreme organs may not hold up as well as the others do in the longer run. But if they work for even ten years in a 70-year-old, they will have done the recipient a great service. And there are other benefits, even for younger patients. Almost any working kidney is better than dialysis, and the use of extreme kidneys means waiting lists shorten by about a year (down from two to six years, depending on the patient's blood group), with a consequent reduction in the risk of dying. Not only that, but the longer a patient remains on dialysis—assuming he survives it—the greater the chance that an eventual transplant will fail. Kidneys may be there to process waste, but “waste not, want not” seems to be the watchword when transplanting them.

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Conservation

Vulture culture

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At last, India's vultures are having their condor moment

IMAGE is everything. Say “condor”, and people get dewy-eyed at the thought of magnificent birds soaring over mountain tops. That such a species could be allowed to become extinct is inconceivable—and, as a consequence, a big, expensive programme to save them is running in California. Say “vulture”, though, and the image is of something up to its neck in carrion. Just like a condor when it is feeding, as it happens. But in the case of vultures, even in a don't-hurt-a-fly, Hindu-majority country like India, it has taken until now to try to stem what is probably the biggest avian population crash since the North American passenger pigeon went from 5 billion to zero between 1870 and 1914.

In 1990 the Indian vulture population was estimated at between 20m and 40m, divided between three species. Now it is about 10,000, and falling by 50% a year. Indeed, one species, the slender-billed vulture, numbers a mere 400. The birds are victims of a drug called diclofenac. This is a non-steroidal anti-inflammatory that was developed to treat people but adopted for cattle in the 1980s. Unfortunately, it causes kidney failure in vultures—and vultures eat a lot of dead cattle. Hence the establishment of the Bombay Natural History Society's vulture-breeding centre at Pinjore, in Haryana.

The centre is intended to create a secure breeding-stock of vultures that may eventually be released into a diclofenac-free wild. It consists of three giant concrete-and-wire aviaries, and is designed to house 75 pairs of each of the three stricken species. At the moment it has 124 vultures, most of them trapped as nestlings in the past two years.

Saving India's vultures from extinction is not merely a sentimental cause, for the birds have a vital role in the country's ecology. India's people share the place with some 200m cattle and buffalo. Yet Indians (Hindu Indians, at least) tend not to eat beef. Until recently, therefore, farmers would leave carcasses where they fell or at local dumps. Within hours, the vultures would have stripped them. With no vultures, these farmers are having to burn or bury the carcasses of fallen cattle—either that, or risk encouraging disease by leaving them to rot.

Another cost of the vultures' decline is that India's feral dog population is booming—bad news for a country that already has 80% of the world's cases of rabies. One carcass dump in Delhi used to sustain 10,000 vultures. In their absence, a similar number of dogs have moved in—not to mention rats.

The vultures also had a third role: clearing human carrion. India (and particularly Mumbai) is home to most of the world's Parsees. The Parsees are Zoroastrians, the theological descendants of ancient Persian fire-worshippers. In Zoroastrianism, the elements are sacred and the body is corrupt. Parsees neither cremate nor bury their dead; rather, corpses are laid out on towers known as *dokhmas* for the vultures to eat. By feeding their dead to the birds of the air, the Parsees profane neither earth nor fire. In the absence of vultures, they have been reduced to rigging their towers with solar reflectors to shrivel the corpses.

Fortunately, there is reason to think that the vulture-preservation effort need not be open-ended. The manufacture of diclofenac for cattle is now banned. It is still used, as people have stocks they are unwilling (and not legally required) to throw away. But there is an acceptable “vulture-safe” alternative called meloxicam, so the hope is that once leftover stocks of diclofenac are exhausted, people will switch to that. Illegal production of diclofenac continues. But the ban has stimulated meloxicam manufacture and its price has fallen by half over the past year.

Even if all does go well, though, it could take 15 years for the country to become safe for wild vultures. Meanwhile, the Bombay Natural History Society is trying to establish another three centres in India, and its counterparts in Pakistan and Nepal may add one each. One of the Indian centres, it has been suggested, could provide vultures for two giant aviaries at the Towers of Silence—the main group of *dokhmas* in Mumbai.

In March a delegation led by Minoo Shroff, the leader of Mumbai's Parsees, visited Pinjore. As he watched the vultures feed, one of Mr Shroff's companions expressed a wish that the meal was of Parsee bodies, not dead goats. But there is a problem: one Parsee corpse containing diclofenac could wipe out a whole aviary of vultures and the Parsees cannot guarantee that this would not happen. The vulture-saving ban on diclofenac does not, of course, extend to people.

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Speciation

A god of small things

Oct 4th 2007
From The Economist print edition

Natural selection in the laboratory creates a new species of virus

FOR most people, the idea of isolation is an uncomfortable one. It interests Paul Turner, however, because it goes hand in hand with the formation of new species. Dr Turner is a biologist at Yale University, and he and his team have just become the first people to create a new biological species in a laboratory by encouraging the sort of ecological isolation that happens in the wild. Admittedly the species in question is a virus, but the proof of principle is important. Moreover, Dr Turner's method might be adapted to examine how animal viruses jump the species barrier to become agents of human disease.

One definition of a species is a group of organisms whose members can breed with each other but not with outsiders. Such groups can form in several ways. One is that a species splits into groups that adapt to different foodstuffs. If those foodstuffs live in different places, the groups will never meet. Since they no longer meet, they no longer interbreed. They have thus become ecologically isolated and natural selection can then drive their genetic make-ups apart.

It has been a source of disappointment to researchers into evolution that although they can replicate the effects of natural selection on individual traits (for example, resistance to pesticides or changes in behaviour), no one has managed to evolve a new species this way. Laboratory species have been created only by the isolating effects of hybridisation. Speciation by hybridisation does happen in the wild, but is exceptional.

As they report in *Evolution*, Dr Turner and his team performed their trick with a type of virus called a bacteriophage. As their name suggests, these infect bacteria. Those the team study can live in more than one bacterial species.

The normal versions of Dr Turner's phages are able to parasitise four types of bacteria. He and his team, however, found a mutant that could infect two additional species. They cultivated a population of this mutant in one of the newly available species and found that after 15 days it had adapted to its new host so well that it had lost the ability to infect other bacteria. It had thus become effectively isolated, because it could never hook up with individuals from other strains. It could therefore be considered a new species.

Bacteria are not people, of course. Neither are phages retroviruses. But what Dr Turner has done is logically equivalent to the step taken by, for example, one particular chimpanzee retrovirus when it leapt to humans and evolved into what is now known as HIV. By showing that viruses can evolve into new species this way in the laboratory, Dr Turner may thus have invented a tool with medical applications. And he has certainly given a psychological boost to evolutionary biologists.

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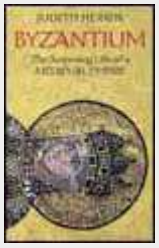
The Byzantine empire

The lasting glory of its art

Oct 4th 2007
From The Economist print edition

And don't forget its vibrant cosmopolitan civilisation

Byzantium: The Surprising Life of a Medieval Empire
By Judith Herrin



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Werner Forman Archive

ON AN unusually mild Arctic morning in September a simply clad but dignified cleric stepped ashore at a remote bay on the southern tip of Greenland and conducted a short service at the remains of the oldest Christian church in the New World. Local Greenlandic worthies were delighted to see the 270th Patriarch of Constantinople, whose ancient office is one of the Byzantine world's enduring bequests to the modern world. As they pointed out, their little church, built in the early 11th century, goes back to the era of an undivided Christendom, which disintegrated a few decades later with the formal split between Rome and Constantinople.

Not all modern observers of Byzantium have been so willing to associate the city on the Bosphorus with universalism or cultural breadth. While Byzantium's rating has risen recently, it has not entirely shaken off the criticisms dished out in the 18th and 19th centuries, including the devastating verdict of William Lecky, an Irish historian, who in 1869 described the Byzantine empire as “the most thoroughly base and despicable form that civilisation has yet assumed.”

Even Byzantium's modern defenders have tended to set out their case in qualified terms, stressing the empire's relationship to other historical developments. Some see it as a connecting line (of debatable effectiveness) between classical antiquity and the modern world; others, particularly those who think that civilisations are doomed perpetually to clash, stress the empire's role as a bulwark against Islam, without which Europe as a whole would have turned Muslim. Others again see it as a catalyst for the European Renaissance, especially after Hellenic talent was freed from Byzantine dogmatism.

Judith Herrin, a professor at King's College London, sets out to show that there are far better reasons to study and admire the civilisation that flourished for more than a millennium before the conquest of Constantinople in 1453, and whose legacy is still discernible all over south-east Europe and the Levant. She presents Byzantium as a vibrant, dynamic, cosmopolitan reality which somehow escaped the constraints of its official ideology. For example, despite the anti-Semitism of the empire's public discourse and theology, its complex, diversified economy could hardly have functioned without the 30-plus Jewish communities that Benjamin of Tudela, a 12th-century rabbi, described.

Ms Herrin also shows that there was a fluid and perpetually evolving relationship between the competing influences of classical Greek learning, Greek Christianity and popular Byzantine culture. She pays particular attention to the powerful female voices that emerged from Byzantium: not just pious ladies who wrote saints' lives and hymns (including one breathtaking piece of sensual, almost erotic religious poetry) but the sophisticated political history that was penned by Anna Komnene, a frustrated would-be empress of the 12th century.

Ms Herrin will certainly win over some sceptics. But it will remain the case that more people are drawn to Byzantine civilisation through its dazzling art and architecture than by its literature. In August 2006, for example, more than 1,000 academic specialists on Byzantium (with contingents from such unlikely places as Tajikistan and Japan) converged on London for a week-long conference. The success of the quinquennial event was a sign that Byzantine studies are flourishing in almost every corner of the world. But it is a reasonable bet that, whatever they ultimately studied, these scholars were first drawn to the Byzantine world by gazing in wonder at an icon or a frescoed church rather than by perusing the pages of Anna Komnene.

The brilliance of Byzantine art is proof enough that something extraordinary happened on the Bosphorus. And this brilliance remained undimmed even when the empire's geopolitical fortunes were collapsing. Snobbish Western classicists who called Byzantium a poor substitute for ancient Greece may have missed the point. True, the Byzantine world was weighed down by deference to classical Greek models. But that charge could also be laid against the pedagogues who used to dominate the study of the humanities in the Western world. Right now, Byzantine history is in vogue at many universities while old-fashioned classical studies are struggling to hold their own.

Byzantium: The Surprising Life of a Medieval Empire
By Judith Herrin
Allen Lane; 416 pages; £20. To be published inJanuary by Princeton University Press; $27.95

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The Korean war

Blundering into battle with China

Oct 4th 2007
From The Economist print edition

SOME old men keep in a half-forgotten file their medal, inscribed with bureaucratic precision: “For service in defence of the principles of the charter of the United Nations”. That was always humbug. The Korean war was an American venture intended to contain the newly victorious Chinese government of Mao Zedong, believed, quite wrongly, to be Moscow's puppet. David Halberstam was too reliable a story-teller to pretend otherwise.

His huge, sadly posthumous book spares just one sentence for the manoeuvre whereby the American delegation whisked the necessary resolution through the UN machine when a brief boycott by Stalin's delegation prevented it from applying its veto. He writes of “UN forces”, barely mentioning those that were not American, and skips through the last two years of static conflict in a couple of pages. His accounts of battles are vivid enough, but exist mainly to add conviction to his central proposition.

His real interest is the sequence of decisions by which America provoked China's intervention and missed chances to end the fighting. The central figure, and villain, is the supreme commander in Tokyo, General Douglas MacArthur. Earlier, MacArthur had brilliantly conducted the war in the Pacific and laid the foundations for the Japanese to build their astonishing state. But, old, stubborn and racially contemptuous of his adversaries, he aligned himself with Washington's “China lobby” and with Chiang Kai-shek's just-defeated nationalist regime. His strategic intelligence was compiled by a fantasist. And he despised his political masters to the point where he refused to salute his commander-in-chief, President Harry Truman.

Mr Halberstam believes that MacArthur, backed by Republican politicians, challenged the constitutional arrangements for civil supremacy that Abraham Lincoln had affirmed during the civil war. The constitution, in its incarnation as Truman, eventually won, and another wartime general, the admirable Dwight Eisenhower, nailed down this victory.

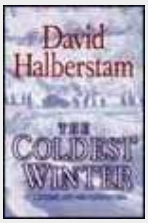
When MacArthur's strategic blunders brought China into the war, the Americans, overwhelmingly superior in technology, armament and logistics, were routed. They clawed their way back, but only to stalemate. The Chinese had no aircraft (Stalin, sensibly enough, had broken his promise to provide them), only such heavy artillery as the retreating Americans abandoned to them and no portable radios to co-ordinate their infantry. At one point, Mr Halberstam claims, their 300,000 men were almost starving, with only 300 trucks for food and ammunition.

But America's soldiers, tied to the valley roads by the weight of their gear and not trained to march, were victims of an enemy that could climb the hills overlooking their rearguard. The Chinese soldiers, even when their commanding hilltops glowed like cigarette-butts beneath tonnes of blazing napalm, would manhandle their mortars from deep-dug shelters and strike with deadly effect. All lessons from old wars were irrelevant.

Plenty of books tell the story of the Korean war. Mr Halberstam understood what it meant for America. Both sides thought they were fighting to unify a divided peninsula. The strange result of their struggle was to create two nations, one rich, the other mad. The world lives precariously with that. No peace treaty has yet put a formal end to the war.

The Coldest Winter: America and the Korean War
By David Halberstam.
Hyperion; 736 pages; $35

The Coldest Winter: America and the Korean War
By David Halberstam



Hyperion; 736 pages; $35

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Arthur Conan Doyle

A man divided

Oct 4th 2007
From The Economist print edition

THE inventor of Sherlock Holmes was the most commercially successful author of his time; by his death in 1930 he was one of the best-known Englishmen in the world. Arthur Conan Doyle was a phenomenon: practising doctor, war correspondent, businessman, politician and a campaigner for legal and colonial reforms as well as a popular novelist. He was a one-man intellectual conglomerate.

But he considered his fiction undervalued. Though he was known worldwide as the author of the Holmes stories and even sometimes addressed as Mr Sherlock Holmes, Doyle (Conan, like Arthur, was his given name) regarded himself as primarily a writer of uplifting historical fiction, usually with a medieval background. At first he considered Sherlock Holmes a pleasant diversion that filled a gap in his income. Eventually he came to think of the detective as an irksome burden: “He keeps me from higher things,” he wrote.

The Sherlock Holmes stories continue to exercise extraordinary power. The writing is never more than efficient but the setting remains perennial: the comfortable, carpeted, fire-lit Baker Street sitting room shared by Holmes and Watson, the paradoxically womblike world of a Victorian bachelor set above an anarchic underworld full of violence and immorality. Doyle's literary masterstroke was dividing the story between Holmes and Watson. It was a device the writer used frequently but never as effectively as here.

Doyle's true theme was division: between order and anarchy, reason and emotion, the material and the spiritual. He himself was a man divided, as two new biographical books make clear. The very picture of an upright Victorian gentleman, Doyle was not averse to fighting in the street when the mood took him. And in his late 30s, at the height of his fame, he ran a double life, conducting a largely secret affair with the woman who eventually became his second wife, while his first was gradually succumbing to tuberculosis.

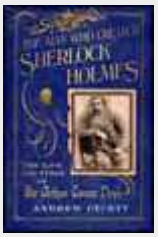
Much of this is revealed in detail in Andrew Lycett's biography and in a selection of Doyle's letters edited by (among others) the present executor of the Doyle estate. The story behind the publication of these two books might make a Doylesque thriller in itself. Mr Lycett and the Doyle estate vied to gain control of newly discovered material, each trying to get to market first (Mr Lycett was just first in Britain; the estate may make it in America).

Mr Lycett's book is a serious piece of work from an experienced professional biographer. If he never quite gets fully to grips with Doyle's elusive personality (which included a mother fixation and a lifelong tendency to be drawn to charismatic cranks and crooks), the author is particularly good on the intellectual background to Doyle's work, both known and forgotten. The biography is hobbled by the Doyle estate's refusal to permit quotation from numerous documents. But Mr Lycett makes the best of what he has and fills the gaps with insight.

The selected letters by contrast are strictly an enthusiast's book. The editors' comments are a bit haphazard and it is poorly presented. On the other hand, it does convey an almost physical presence of the author, with his strange mixture of kindness and carelessness, overbearing self-confidence and depressive self-doubt.

Above all there is the impression of a man driven by internal forces. Since boyhood Doyle had been

Conan Doyle: The Man who Created Sherlock Holmes
By Andrew Lycett



To be published in December by Free Press; $30
Weidenfeld & Nicholson; 432 pages; £20

Buy it at
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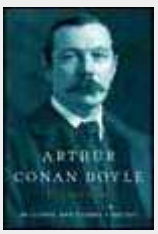
Arthur Conan Doyle: A Life in Letters
Edited by Jon Lellenberg, Daniel Stashower and Charles Foley



Published in November by The Penguin Press; $37.95
Harper Press; 710 pages; £25

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struggling with the consequences of his rationalist rejection of Catholicism and his growing conviction that there must be some kind of reality beyond the scientific. This was a division that in the end he could not manage. By the close of his life he was spending his diminishing energies defending not only the world of spiritualism but also the outermost fraudulent fringes of supernatural belief. It was a sorry ending.

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By Andrew Lycett.
Weidenfeld & Nicholson; 432 pages; £20.
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Philanthropy

The secretive do-gooder

Oct 4th 2007
From The Economist print edition

FOR most of his life Chuck Feeney has guarded his privacy obsessively. When he became a philanthropist, his gifts came on condition that his name never appeared on any press release or plaque; all donations would cease if confidentiality was breached. But when he decided to co-operate with Conor O'Clery on this book, many of the people in his life, released from their Trappist vows, let themselves go. The result is gripping.

An Irish-American, born in New Jersey in 1931, Mr Feeney made a fortune by co-founding Duty Free Shoppers (DFS) which first sold tax-exempt goods to American soldiers abroad and then tapped into the rise of mass tourism. When DFS was sold in 1997, it had delivered nearly $8 billion to its four main shareholders, of which Mr Feeney was the joint biggest, with 38.75% .

Tax avoidance is the flip side to Mr Feeney's philanthropic coin. He is addicted to it. “Chuck hates taxes. He believes people can do more with money than governments can,” says a friend. In 1964 a young New York lawyer, Harvey Dale, told Mr Feeney that changes in the tax laws threatened his business, which was running risks that could put the founders in jail. On his advice, Mr Feeney and his co-founder, Robert Miller, transferred ownership to their foreign-born wives, from France and Ecuador, respectively.

The Billionaire Who Wasn't: How Chuck Feeney Secretly Made and Gave Away a Fortune
By Conor O'Clery

Public Affairs; 338 pages; $26.95; Perseus Books; £15.99

Buy it at
Amazon.com
Amazon.co.uk

In 1974, through a deal with the American government, the firm turned the Pacific island of Saipan into a tax haven. Then, in 1978, Mr Feeney grouped his various investments, including his shares of DFS, in a holding company, General Atlantic Group Limited, in tax-free Bermuda. To escape the American taxman, everything was still registered in his wife's name.

Mr Feeney carefully shunned all outward evidence of wealth. But as soon as DFS became reliably profitable, he started the practice of giving 5% of his pre-tax profits to good causes. In 1982 he created a foundation, the Atlantic Philanthropies, based in Bermuda. Two years later he signed over his fortune to the foundation, except for sums set aside for his wife and children. His net worth fell below $5m. When he broke the news to his children, he gave them each a copy of Andrew Carnegie's essay on wealth, written in 1889.

Mr Feeney has given his alma mater, Cornell University, more than $600m, dwarfing all other donations from a single alumnus to an American university. He has contributed hundreds of millions of dollars towards higher education in Ireland, South Africa and Australia. He has helped with health care in Vietnam. In 2004 he went to Cuba, where he met Fidel Castro, who seemed only too happy to accept his capitalist-tax-avoided dollars. But it was his support for the Irish peace process that caused the most controversy, including accusations (without foundation, it turned out) that he had financed the IRA.

Mr Feeney is committed to giving away all the money in his foundation by a fixed date—thought to be in about ten years—but his investment prowess makes this difficult. Currently, Atlantic Philanthropies is worth $4 billion (up from $3.5 billion in 2001) even though, over its lifetime, it has given away about $4 billion in increasing amounts. The trouble for Mr Feeney is that the foundation's assets are growing as fast as he tries to get rid of them.

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Royal intrigue

Gambling lady

Oct 4th 2007
From The Economist print edition

TRACY BORMAN can tell a good story. Admittedly, her subject is a gift. But Henrietta Howard, mistress to George II, lived in the midst of a large cast of characters, many of them entangled in the complicated politics of 18th-century court life, and Ms Borman handles them and their world with aplomb.

Though the 18th century is called the Age of Reason, it was anything but. Henrietta was born in 1689, a year after the balance of power in Britain shifted from monarch to Parliament. But this did nothing to shift the tyranny of men over women, and Henrietta's life was largely shaped by violent and unreasonable men.

When she was eight, her father, the profligate and choleric squire of Blickling Hall in Norfolk, challenged a neighbour to a duel for impugning his valour. He was killed for his pains, leaving a wife, eight children and a pile of debts. Eight years later, perhaps hoping to help her now motherless siblings, Henrietta released her dowry money by marrying a cousin, Charles Howard, 14 years her senior.

Henrietta Howard: King's Mistress, Queen's Servant
By Tracy Borman

Jonathan Cape; 324 pages; £20

Buy it at Amazon.co.uk

It was a disaster. Charles turned out to be a compulsive gambler and wife-beater, and their lives descended into lodging-house flits and near-starvation. Then, aged 25, Henrietta made her own astonishing gamble. In 1714, when Queen Anne lay dying, she took herself and Charles off to Hanover, where George Louis, heir presumptive to the English throne, held court. There she joined throngs of other hopefuls, all jockeying for the notice either of George Louis, or his son, George Augustus, or his daughter-in-law, Caroline.

Henrietta's gamble paid off, though frying pans and fires come to mind. Her appointment as Woman of the Bedchamber to Princess Caroline meant long days of tedious and exacting ceremony, such as holding her mistress's wash basin on bended knee, a point that Caroline spitefully insisted on when Henrietta became her husband's mistress. Not that that was much comfort either. The man was a boor, and dull with it. In any case, Henrietta never really supplanted Caroline. Being a royal mistress was, in this case, more a post than a romance. But it suited Henrietta in that it protected her from her husband—something the law denied her.

Henrietta was known for her discreet and even temper, but she must also have had sharp elbows. As Ms Borman vividly shows, the court was a scandal-mongering, fickle place, riven by political factionalism and held at fever pitch by the royal family's own very public quarrels. This was the atmosphere Henrietta breathed. And yet she somehow managed to be liked. Even acid-tongued poet, Alexander Pope, described her as reasonable, good-humoured, witty and, above all, a friend.

Some of Ms Borman's most engaging writing describes Henrietta's circle of friends—poets, writers and wits such as Lord Chesterfield and Horace Walpole—and the pleasure they all took in the design of her Palladian villa, Marble Hill at Twickenham. When her husband's death made it safe for her to retire, this was where she came: to entertain, to re-marry, to have a home. After a life of winging it, such hard-wrung domesticity feels almost heroic.

Henrietta Howard: King's Mistress, Queen's Servant
By Tracy Borman.
Jonathan Cape; 324 pages; £20

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Olafur Eliasson

Spinning tops and frozen cars

Oct 4th 2007
From The Economist print edition

I'm a people lover, not a nature lover, says this Scandinavian artist

WHEN asked to describe his work, Olafur Eliasson, replies “My art is about you.” This might sound strange, coming from an artist who is famous for creating a giant artificial sun at Tate Modern, who has just built a pavilion that looks like a spinning top in London's Hyde Park and is showing pieces ranging from a rainbow to a frozen hydroelectric car in his new retrospective at San Francisco's Museum of Modern Art. But for Mr Eliasson, the viewer's interaction with his art is an essential part of it.

For the past 15 years, the artist, born in Denmark in 1967 to Icelandic parents and now based in Berlin, has been quietly creating what might be called total-immersion art. “I make art that creates an experience, not a representation,” he says. For instance, he has dyed rivers green in cities from Stockholm to Tokyo in order to stimulate people to look afresh at their urban surroundings.

His show at San Francisco (which is there until February, goes on to New York and Dallas and will be in Sydney by the summer of 2009) includes walk-in kaleidoscopes and installations of mist, clouds and backward-flowing waterfalls, walls made of moss, sculptures of wood and mushrooms, and floors of compressed soil. He aspires to create art that is recyclable, made of sustainable materials.

As he walks up the ramp of the new pavilion he has co-designed with a Norwegian firm, Snohetta Architects, at London's Serpentine Gallery, he speaks with messianic fervour about his mission to engage people through art: “I want to create art that allows people to be singular and plural, to have an individual experience...and at the same time engage with other people and the landscape around them.” The pavilion (open until November 5th) is designed in a way that defies representation: it doesn't photograph well and can't be described in a sound-bite. The only way to understand it is by experiencing it.

The central element is a ramp, which Mr Eliasson has emphasised by spiralling it around the building from the ground to the roof, giving viewers panoramic vistas of the park as they ascend, and a panoptic vision of the interior when they reach the top. Inside he has created a grotto-like space, where amphitheatre seating curves around to meet the walls. An oculus in the ceiling lets in a diagonal shaft of light while low-energy lamps emit reddish beams. It looks like a wacky, 21st-century twist on the Baroque.

Mr Eliasson believes that art today has an unprecedented opportunity to effect social change. “When I was a student, people became artists to step away from the world; now it is a way to engage with it.” Seeing indifference and homogeneity in public life, he wonders: “Why do people no longer have faith in basic social interaction? How does the individual fit within the collective?” Mr Eliasson constantly poses such questions in his work.

His interests in aesthetics and ethics converge in his new design for a hydroelectric car for BMW on show in San Francisco. Displayed in a chilled room, the car is encased in a translucent steel mesh covered in ice. Literally frozen in its tracks (though it has been known accidentally to melt), the vehicle is a reflection on the relationship between the car industry and global warming. The ice calls attention to the fact that hydrogen becomes fuel-ready only at sub-zero temperatures.

When asked how he squares his work for companies such as BMW with his antipathy to corporate values, he admits ambivalence. Nonetheless, he says, “I live in this world, not a parallel universe, and I have to engage with it.” He funnels the money he makes from such projects into his charitable foundation, 121ethiopia.org, which finances orphanages in Ethiopia.

Mr Eliasson's Scandinavian roots are often cited as an inspiration for his green politics and his use of natural elements. But he rejects this, insisting that he is not obsessed with clichés about the purity of the

Nordic environment. “I am not a nature lover, I am a people lover. That is why I am an artist: I use art to engage people.”

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Haidar Abdel Shafi

Oct 4th 2007
From The Economist print edition

Haidar Abdel Shafi, a model for the Palestinians, died on September 25th, aged 88

Corbis

IN THE spring of 1948, around March as he remembered it, Haidar Abdel Shafi found himself at nightfall, waiting, in a small mud hut by the side of the main road in Deir al-Balah. Around him stretched groves of olive and orange trees. Palestine, in those days, was a community of peasants and landowners; a man was judged by how many trees he had. Haidar's father had had none, preferring—as he told the astonished neighbours—to save money for schooling his six children rather than buy plantations. The lanky boy, with his dark brows, had shaken the dust from his feet and gone away to study. But he was back now, defending the land.

Beside him lay a bag of first-aid equipment. He was a doctor, trained in Beirut and Jerusalem, now based in Gaza, and one of only about a dozen practising in the whole southern sector of Palestine. With his few colleagues he had founded, in 1945, a southern branch of the Palestine Medical Society, and together they had attended the first Palestine Medical Congress. Since his student days, when he had first been inspired by Arab pan-nationalism, he had looked on doctoring as a form of resistance: to illness, to poverty and, by strengthening the common people, to political troubles and oppressions. When it came to organising Palestinians, a community not easily made coherent, a network of doctors, clinics and waiting rooms might serve as well as any political party. But crouching in a hut by the main road was not his normal mode of operation.

Somewhere ahead of him were a group of *fedayeen*, Arab guerrilla fighters, who had come to attack the Jewish settlement of Kfar Darom. The settlement, one of many built on purchased land in Palestine in the years before the establishment of Israel, was well-defended, surrounded by circle after circle of barbed wire. Within the circles the ground was mined, and the whole scene was overlooked by Jewish observation towers.

The battle, though it raged all night, was a bloody defeat for the *fedayeen*: 12 killed, with Dr Abdel Shafi's first-aid bag no match for the mines and the snipers. The Zionists seemed superbly organised. Indeed, it was usually so. All through his long career, in which he was a founder-member of the Palestine Liberation Organisation (PLO) and represented Gaza on the Palestinian Legislative Council (PLC), the doctor's chief lament about his own people was their disarray. They had little notion of democracy, being loyal instead to Yasser Arafat, a strongman who monopolised all decision-making and surrounded himself with thieves. And they turned out in the end to have no capacity for national unity, splintering into factions—Hamas, Fatah, Islamic Jihad and the rest—who then fought one another. The Israelis, as he often pointed out, needed only to watch the Palestinians destroy themselves, as they had watched that March night from their high, dark towers.

Requiem for the olive trees

Dr Abdel Shafi was that rarest of figures, a secular and non-sectarian Palestinian leader whose integrity and outspokenness made him a model for all the rest. He was of the left, in an old socialist way, but was never a member of the Popular Front for the Liberation of Palestine; a doctor's role, he seemed to believe, was to stay detached from such affiliations. Far more useful was his decision to found and direct the Gaza branch of the Red Crescent, his own rallying organisation for Palestinian improvement. The Islamists attacked him, and in 1981 burned his clinic down; he noted then, stoically, that the Israelis who then ruled Gaza did not trouble to intervene.

On both the PLO and the PLC he was a gadfly, denouncing corruption and resigning with much publicity from the PLC, in 1997, because it was doing nothing to counter Israeli ambitions. The Palestinian Authority infuriated him because it would not control the *intifada* and was allowing Palestinians (though, he stressed, they had every reason to rebel) to commit random violence against Jewish civilians. He never ran for president in the 1996 elections, but might have done well if he had.

Though the Israelis twice deported him and then confined him to Gaza for his long-term refusal to co-operate, he did not oppose the existence of Israel. The Jewish presence was a reality, and the Jewish state had to be accepted. Nor did he dislike Jews: at Sabbath dusks, as a boy, he had been in demand to light the lamps of his Jewish neighbours. But there had to be a spirit of “mutuality and reciprocity”: two viable states, side by side, within the 1967 borders, and no Jewish settlers on Palestinian land. Until the settlements stopped entirely, he insisted, there was no point in any peace plan for the Middle East.

This was his message at the Madrid Conference in 1991 and at the Washington talks that followed—talks which he led and which were undermined, to his disgust, by secret accords made later at Oslo between Arafat and the Israelis. His speech at Madrid was perhaps the most eloquent the West had ever heard from a Palestinian: a plea for understanding, for sympathy and for territory. “What requiem can be sung”, he asked, “for trees uprooted by army bulldozers? And...who can explain to those whose lands are confiscated and clear waters stolen, a message of peace? Remove the barbed wire. Restore the land.”

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Overview

Oct 4th 2007
From The Economist print edition

American manufacturing grew more slowly in September, according to the Institute for Supply Management. Its activity index slipped to 52 from 52.9 in August.

Consumer prices in the **euro area** rose by 2.1% in the year to September, according to a preliminary estimate, sharply faster than the 1.7% in the year to August. The currency zone's unemployment rate was 6.9% in August, unchanged from July.

Australia's central bank left its benchmark interest rate at 6.5% on October 2nd.

Manufacturers in **Japan** remain confident despite recent gyrations in financial markets, according to the central bank's quarterly Tankan survey. The percentage balance of large firms reporting “favourable” over “unfavourable” business conditions was 23, the same as in June.

Industrial production in **South Korea** rose by 11.2% in the year to August, thanks to strong global demand for its cars, semiconductors and machinery goods. Consumer prices rose by 2.3% in the year to September.

In **Britain** the number of loans approved for purchasing homes dropped to 109,000 in August from 115,000 in July.

The outlook for rich-world economies is gloomier, according to the *The Economist's* **monthly poll of forecasters** (see article). Forecasts for GDP growth in 2008 have been marked down in most countries. The one exception is Australia.

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Output, prices and jobs

Oct 4th 2007
From The Economist print edition

Output, prices and jobs

% change on year ago

	Gross domestic product				Industrial production	Consumer prices			Unemployment
	latest	qtr*	2007†	2008†	latest	latest	year ago	2007†	rate‡, %
United States	+1.9 Q2	+4.0	+2.0	+2.2	+1.7 Aug	+2.0 Aug	+3.8	+2.8	4.6 Aug
Japan	+1.6 Q2	−1.2	+2.0	+1.9	+4.3 Aug	−0.2 Aug	+0.9	nil	3.8 Aug
China	+11.9 Q2	na	+10.5	+9.6	+17.5 Aug	+6.5 Aug	+1.3	+3.0	9.5 2006
Britain	+3.1 Q2	+3.3	+2.9	+2.1	+0.9 Jul	+1.8 Aug§	+2.5	+2.3	5.4 Jul††
Canada	+2.5 Q2	+3.6	+2.5	+2.5	−0.5 Jul	+1.7 Aug	+2.1	+2.2	6.0 Aug
Euro area	+2.5 Q2	+1.4	+2.6	+2.1	+3.7 Jul	+2.1 Sep	+1.7	+2.0	6.9 Aug
Austria	+3.7 Q2	+4.0	+3.2	+2.6	+5.3 Jul	+1.7 Aug	+1.8	+1.8	4.2 Sep
Belgium	+2.9 Q2	+2.5	+2.6	+2.1	+3.3 Jul	+1.5 Sep	+1.2	+1.7	11.9 Aug‡‡
France	+1.3 Q2	+1.3	+1.8	+2.0	+2.6 Jul	+1.2 Aug	+1.9	+1.4	8.0 Jul
Germany	+2.5 Q2	+1.0	+2.7	+2.2	+4.4 Jul	+2.5 Sep	+1.0	+2.0	8.8 Sep
Greece	+4.1 Q2	na	+3.8	+3.2	+3.5 Jul	+2.5 Aug	+3.5	+2.6	8.2 Jun
Italy	+1.8 Q2	+0.5	+1.8	+1.5	−0.2 Jul	+1.7 Sep	+2.1	+1.9	6.0 Q2
Netherlands	+2.6 Q2	+1.2	+2.5	+2.2	+4.1 Jul	+1.3 Sep	+1.3	+1.6	4.5 Aug††
Spain	+4.0 Q2	+3.8	+3.7	+2.7	+4.0 Jul	+2.2 Aug	+3.7	+2.7	8.0 Aug
Czech Republic	+6.0 Q2	+5.7	+5.7	+4.2	+11.5 Jul	+2.4 Aug	+3.1	+2.6	6.4 Aug
Denmark	+0.6 Q2	−1.6	+1.7	+1.8	nil Jul	+1.1 Aug	+2.0	+1.7	3.3 Aug
Hungary	+1.2 Q2	+0.2	+2.4	+3.0	+9.4 Jul	+8.3 Aug	+3.5	+7.5	7.2 Aug††
Norway	+3.9 Q2	+3.5	+3.1	+2.6	+2.9 Jul	+0.4 Aug	+1.9	+0.8	2.5 Jul††
Poland	+6.7 Q2	na	+6.5	+5.1	+9.0 Aug	+1.5 Aug	+1.6	+2.3	12.0 Aug‡‡
Russia	+7.8 Q2	na	+6.7	+6.2	+3.8 Aug	+8.7 Aug	+9.7	+7.8	5.7 Aug‡‡
Sweden	+3.5 Q2	+3.7	+3.4	+3.0	+5.2 Jul	+1.8 Aug	+1.6	+1.8	4.8 Aug‡‡
Switzerland	+2.8 Q2	+3.0	+2.6	+2.1	+9.8 Q2	+0.7 Sep	+0.8	+0.7	2.6 Aug‡‡
Turkey	+3.9 Q2	na	+5.6	+5.3	+3.9 Jul	+7.1 Sep	+10.6	+8.7	8.9 Q2‡‡
Australia	+4.3 Q2	+3.8	+4.1	+3.5	+5.5 Q1	+2.1 Q2	+4.0	+2.4	4.3 Aug
Hong Kong	+6.9 Q2	+8.2	+6.2	+5.2	−2.3 Q2	+1.6 Aug	+2.5	+1.9	4.2 Aug††
India	+9.3 Q2	na	+8.4	+7.9	+7.1 Jul	+6.5 Jul	+6.7	+5.7	7.6 2006
Indonesia	+6.3 Q2	na	+6.3	+6.4	+3.9 Jul	+7.0 Sep	+14.5	+6.1	9.8 Feb
Malaysia	+5.7 Q2	na	+6.0	+5.8	+2.1 Jul	+1.9 Aug	+3.3	+2.1	3.4 Q2
Pakistan	+6.6 2006**	na	+6.4	+5.9	+6.0 Jun	+6.5 Aug	+8.9	+6.7	6.2 2006††
Singapore	+8.6 Q2	+14.0	+7.0	+5.1	+13.8 Aug	+2.9 Aug	+0.7	+1.2	2.4 Q2
South Korea	+5.0 Q2	+7.4	+4.9	+5.2	+11.2 Aug	+2.3 Sep	+2.5	+2.3	3.2 Aug
Taiwan	+5.1 Q2	na	+4.3	+4.6	+10.2 Aug	+1.6 Aug	−0.6	+1.0	3.9 Aug
Thailand	+4.4 Q2	+5.2	+4.6	+5.0	+7.2 Jul	+2.1 Sep	+2.7	+2.0	1.6 Jun
Argentina	+8.7 Q2	+8.8	+7.7	+5.7	+0.1 Aug	+8.7 Aug	+10.7	+8.6	8.5 Q2‡‡
Brazil	+5.4 Q2	+3.2	+4.7	+4.5	+6.8 Jul	+4.2 Aug	+3.8	+3.7	9.5 Aug‡‡
Chile	+6.1 Q2	+6.5	+6.1	+5.1	+4.0 Aug	+5.8 Sep	+2.8	+3.7	7.6 Aug†††‡
Colombia	+6.9 Q2	+4.4	+6.6	+5.8	+12.4 Jul	+5.0 Sep	+4.6	+5.6	11.1 Jun‡‡
Mexico	+2.8 Q2	+5.3	+2.9	+3.2	+2.4 Jul	+4.0 Aug	+3.5	+4.0	3.9 Aug‡‡
Venezuela	+8.9 Q2	na	+6.7	+4.0	+11.2 Jun	+15.3 Sep	+15.3	+18.1	8.4 Q2‡‡
Egypt	+7.4 Q1	na	+7.0	+7.3	+10.5 2006	+8.5 Aug	+8.9	+8.4	9.0 Q1‡‡
Israel	+4.4 Q2	+6.1	+5.0	+4.5	+3.1 Jul	+1.0 Aug	+2.2	+0.5	7.6 Q2
Saudi Arabia	+4.3 2006†	na	+4.8	+5.6	na	+4.4 Aug	+1.6	+3.4	na
South Africa	+5.0 Q2	+4.5	+4.8	+5.1	+3.1 Jul	+6.7 Aug	+5.4	+6.0	25.5 Mar‡‡
MORE COUNTRIES Data for the countries below are not provided in printed editions of *The Economist*									
Estonia	+7.6 Q2	na	+7.9	+5.8	+4.4 Aug	+5.7 Aug	+5.0	+6.0	5.4 Jul
Finland	+4.7 Q2	+3.8	+4.4	+2.7	−0.3 Aug	+2.3 Aug	+1.9	+2.7	6.9 Aug
Iceland	+2.5 Q2	+9.1	+1.2	+1.6	+7.6 2006	+4.2 Sep	+7.6	+4.8	0.9 Aug‡‡
Ireland	+5.4 Q2	−5.5	+4.8	+3.4	+13.9 Jul	+4.8 Aug	+4.4	+4.7	4.7 Aug
Latvia	+11.3 Q2	na	+9.6	+7.5	+1.8 Jul	+10.1 Aug	+6.8	+8.8	5.6 Jul
Lithuania	+8.0 Q2	+8.2	+7.8	+6.9	na	+4.6 Aug	+4.2	+4.6	2.8 Aug
Luxembourg	+6.2 Q1	+6.6	+5.2	+4.3	+4.0 Jun	+1.9 Aug	+2.8	+2.2	4.1 Jul‡‡
New Zealand	+3.8 Q2	+3.4	+3.0	+3.0	nil Q1	+2.0 Q2	+4.0	+2.4	3.6 Q2
Peru	+8.4 Jul	na	+7.1	+5.5	+12.1 Jul	+2.8 Sep	+2.0	+1.2	8.2 Jul‡‡
Philippines	+7.5 Q2	+7.1	+6.0	+5.6	+0.6 Jul	+2.4 Aug	+6.3	+2.9	7.8 Q3‡‡
Portugal	+1.6 Q2	+1.7	+1.8	+2.1	+1.0 Aug	+2.1 Aug	+2.9	+2.4	7.9 Q2‡‡
Slovakia	+9.4 Q2	na	+8.0	+6.0	+18.9 Jul	+2.3 Aug	+5.1	+2.7	8.2 Aug
Slovenia	+5.9 Q2	na	+5.6	+4.6	+8.9 Jul	+3.5 Sep	+2.5	+3.0	7.6 Jul‡‡

*% change on previous quarter, annual rate. †*The Economist* poll or Economist Intelligence Unit estimate/forecast. ‡National definitions. §RPI inflation rate 4.1% in Aug. **Year ending June. ††Latest three months. ‡‡Not seasonally adjusted.

Sources: National statistics offices and central banks; Thomson Datastream; Reuters; Centre for Monitoring Indian Economy; OECD; ECB

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The Economist commodity-price index

Oct 4th 2007
From The Economist print edition

The Economist commodity-price index

2000=100

	Sep 25th	Oct 2nd*	% change on one month	% change on one year
Dollar index				
All items	216.5	216.8	+6.5	+25.7
Food	197.7	196.7	+6.4	+44.1
Industrials				
All	240.9	242.9	+6.7	+10.8
Nfa†	166.6	165.6	+2.9	+21.4
Metals	281.4	285.1	+7.9	+7.9
Sterling index				
All items	162.9	161.1	+4.9	+16.3
Euro index				
All items	141.8	141.7	+2.3	+13.1
Gold				
$ per oz	728.65	728.80	+7.1	+25.1
West Texas Intermediate				
$ per barrel	79.53	80.23	+6.8	+36.8

*Provisional †Non-food agriculturals.

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The Economist poll of forecasters, October averages

Oct 4th 2007
From The Economist print edition

The Economist poll of forecasters, October averages (previous month's, if changed)

	Real GDP, % change Low/high range		Real GDP, % change average		Consumer prices % increase		Current account % of GDP	
	2007	2008	2007	2008	2007	2008	2007	2008
Australia	3.5/4.4	3.0/4.3	4.1 (3.8)	3.5 (3.4)	2.4	2.8	–5.7 (–5.4)	–5.4 (–5.1)
Belgium	2.4/2.8	1.9/2.5	2.6	2.1 (2.3)	1.7 (1.8)	1.8	2.2	2.1
Britain	2.7/3.2	1.6/2.5	2.9	2.1 (2.4)	2.3 (2.4)	2.0	–3.2 (–3.3)	–3.1 (–3.2)
Canada	2.2/2.9	2.0/2.9	2.5	2.5 (2.7)	2.2 (2.4)	2.2 (2.3)	1.8 (1.6)	1.5 (1.4)
France	1.7/2.0	1.5/2.2	1.8 (2.0)	2.0 (2.2)	1.4 (1.5)	1.7 (1.8)	–1.2	–1.1
Germany	2.4/3.0	1.9/2.5	2.7 (2.8)	2.2 (2.3)	2.0	1.6 (1.7)	5.4 (5.1)	5.3 (5.1)
Italy	1.3/2.0	1.0/1.8	1.8 (2.0)	1.5 (1.7)	1.9	1.9 (2.0)	–2.4 (–2.3)	–2.2 (–2.1)
Japan	1.8/2.4	1.5/2.5	2.0 (2.4)	1.9 (2.2)	nil	0.3	4.6 (4.4)	4.5
Netherlands	2.4/2.8	1.8/2.6	2.5 (2.7)	2.2 (2.6)	1.6 (1.8)	1.9 (2.0)	7.9	7.5 (7.8)
Spain	3.3/4.0	2.4/3.1	3.7	2.7 (2.8)	2.7	2.8 (2.9)	–9.0 (–8.8)	–8.5 (–8.3)
Sweden	3.2/4.0	2.7/3.5	3.4 (3.5)	3.0 (3.2)	1.8	2.1	6.9 (6.8)	6.6 (6.5)
Switzerland	2.4/2.7	1.7/2.4	2.6 (2.4)	2.1	0.7	1.1 (1.2)	16.4 (16.1)	16.0 (15.5)
United States	1.9/2.1	1.3/2.6	2.0	2.2 (2.6)	2.8 (2.7)	2.4	–5.6 (–5.7)	–5.2 (–5.5)
Euro area	2.5/2.8	1.7/2.3	2.6 (2.7)	2.1 (2.3)	2.0	2.0	0.2	nil 0.3 (0.2)

Sources: ABN AMRO, BNP Paribas, Citigroup, Decision Economics, Deutsche Bank, Economist Intelligence Unit, Goldman Sachs, HSBC Securities, KBC Bank, JPMorgan Chase, Morgan Stanley, Scotiabank, UBS

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Trade, exchange rates, budget balances and interest rates

Oct 4th 2007
From The Economist print edition

Trade, exchange rates, budget balances and interest rates

	Trade balance* latest 12 months, $bn	Current-account balance latest 12 months, $bn	Current-account balance % of GDP 2007†	Currency units, per $ Oct 3rd	Currency units, per $ year ago	Budget balance % of GDP 2007†	Interest rates, % 3-month latest	Interest rates, % 10-year gov't bonds, latest
United States	−818.7 Jul	−793.2 Q2	−5.6	–	–	−1.6	4.81	4.54
Japan	+93.2 Jul	+192.6 Jul	+4.6	117	118	−2.5	0.73	1.69
China	+244.9 Aug	+249.9 2006	+10.7	7.51	7.90	−0.7	3.85	4.65
Britain	−158.6 Jul	−86.6 Q2	−3.2	0.49	0.53	−2.7	6.20	4.99
Canada	+47.9 Jul	+21.9 Q2	+1.8	1.00	1.13	0.6	3.97	4.34
Euro area	+29.2 Jul	+11.2 Jul	+0.2	0.71	0.79	−0.7	4.80	4.33
Austria	+1.3 Jul	+13.2 Q1	+2.9	0.71	0.79	−0.5	4.79	4.42
Belgium	+17.6 Jul	+14.4 Jun	+2.2	0.71	0.79	−0.1	4.86	4.46
France	−40.1 Jul	+15.8 Jul	−1.2	0.71	0.79	−2.4	4.79	4.44
Germany	+228.1 Jul	+192.3 Jul	+5.4	0.71	0.79	0.4	4.79	4.33
Greece	−47.8 Jun	−36.7 Jul	−10.5	0.71	0.79	−2.4	4.79	4.61
Italy	−16.3 Jul	−49.4 Jul	−2.4	0.71	0.79	−2.5	4.79	4.58
Netherlands	+49.0 Jul	+53.5 Q2	+7.9	0.71	0.79	−0.6	4.79	4.41
Spain	−123.8 Jul	−122.3 Jun	−9.0	0.71	0.79	1.7	4.79	4.43
Czech Republic	+3.1 Jul	−4.5 Jul	−3.5	19.5	22.3	−4.1	3.49	4.49
Denmark	+4.8 Jul	+4.7 Jul	+1.5	5.27	5.88	3.8	4.90	4.44
Hungary	−1.9 Jul	−6.8 Q2	−5.2	178	217	−6.0	7.44	6.58
Norway	+53.3 Aug	+54.6 Q2	+14.2	5.43	6.62	18.9	5.59	4.90
Poland	−9.2 Jul	−12.6 Jul	−3.3	2.67	3.10	−2.2	5.09	5.71
Russia	+121.4 Aug	+73.3 Q3	+6.8	25.0	26.8	3.0	10.00	6.34
Sweden	+18.1 Aug	+29.7 Q2	+6.9	6.50	7.35	2.4	3.60	4.32
Switzerland	+11.1 Aug	+102.1 Q1	+16.4	1.18	1.25	0.3	2.80	2.91
Turkey	−56.4 Aug	−33.2 Jul	−7.3	1.20	1.51	−2.8	6.68	6.91§
Australia	−13.0 Aug	−47.1 Q2	−5.7	1.13	1.35	1.3	6.86	6.14
Hong Kong	−20.6 Aug	+25.3 Q2	+10.9	7.76	7.79	1.8	5.19	4.16
India	−70.7 Aug	−9.7 Q2	−1.4	39.6	45.7	−3.3	7.17	8.29
Indonesia	+41.7 Aug	+11.1 Q2	+2.3	9,124	9,220	−1.7	8.15	6.52§
Malaysia	+28.7 Aug	+25.9 Q1	+13.8	3.41	3.69	−3.2	3.62	5.06§
Pakistan	−13.6 Aug	−6.8 Q1	−4.5	60.7	60.6	−4.6	9.75	8.54§
Singapore	+38.1 Aug	+41.6 Q2	+25.7	1.48	1.58	0.3	2.44	2.71
South Korea	+20.1 Sep	+6.9 Jul	+0.4	914	949	0.5	5.34	5.53
Taiwan	+14.3 Aug	+28.3 Q2	+6.3	32.6	33.1	−2.0	2.60	2.71
Thailand	+10.2 Aug	+11.5 Jul	+3.5	34.2	37.6	−1.9	3.55	4.33
Argentina	+10.2 Aug	+7.4 Q2	+3.5	3.15	3.10	1.5	12.94	na
Brazil	+43.1 Sep	+10.6 Aug	+0.7	1.82	2.17	−1.8	11.18	6.16§
Chile	+24.4 Aug	+8.3 Q2	+3.3	505	535	8.0	5.88	5.10§
Colombia	−1.5 Jun	−4.1 Q1	−3.0	2,013	2,405	−0.2	8.77	6.10§
Mexico	−1.2 Aug	−7.0 Q2	−1.0	10.9	11.1	0.1	7.19	7.85
Venezuela	+23.8 Q2	+20.4 Q2	+8.1	2,147	2,807	−2.6	11.00	6.55§
Egypt	−14.1 Q1	+3.1 Q1	+2.3	5.58	5.74	−5.5	7.21	5.41§
Israel	−9.0 Aug	+7.8 Q2	+3.4	4.01	4.27	−0.9	4.25	5.18
Saudi Arabia	+146.6 2006	+98.9 2006	+23.3	3.74	3.75	18.7	5.08	na
South Africa	−9.6 Aug	−17.4 Q2	−6.3	6.89	7.95	0.5	10.40	8.23
MORE COUNTRIES Data for the countries below are not provided in printed editions of *The Economist*								
Estonia	−4.0 Jul	−3.1 Jul	−16.3	11.1	12.3	3.2	5.20	na
Finland	+12.5 Jul	+12.3 Jul	+6.2	0.71	0.79	4.2	4.63	4.41
Iceland	−1.8 Aug	−3.7 Q2	−16.7	61.3	68.6	3.7	13.99	na
Ireland	+36.2 Jul	−10.5 Q2	−5.1	0.71	0.79	1.0	4.79	4.40
Latvia	−7.0 Jul	−6.0 Jul	−22.2	0.50	0.55	nil	11.41	na
Lithuania	−6.5 Jul	−4.3 Jul	−12.9	2.44	2.72	−0.5	5.64	na
Luxembourg	−5.6 Jun	+4.5 Q1	na	0.71	0.79	0.3	4.79	na
New Zealand	−4.5 Aug	−9.3 Q2	−8.2	1.32	1.51	4.8	7.15	6.28
Peru	+8.8 Jul	+2.8 Q2	+1.9	3.02	3.25	0.4	5.00	na
Philippines	−3.0 Jul	+6.4 Jun	+5.1	45.1	50.0	−1.1	6.94	na
Portugal	−23.3 Jun	−18.0 Jun	−8.6	0.71	0.79	−3.2	4.79	4.55
Slovakia	−2.8 Jul	−3.5 May	−4.5	24.2	29.3	−2.9	4.13	4.63
Slovenia	−2.4 Jul	−1.5 Jun	−2.6	0.71	0.79	−1.2	na	na

*Merchandise trade only. †*The Economist* poll or Economist Intelligence Unit forecast. ‡Dollar-denominated bonds.

Sources: National statistics offices and central banks; Thomson Datastream; Reuters; JPMorgan; Bank Leumi le-Israel; Centre for Monitoring Indian Economy; Danske Bank; Hong Kong Monetary Authority; Standard Bank Group; UBS; Westpac.

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Markets

Oct 4th 2007
From The Economist print edition

Markets

	Index Oct 3rd	% change on one week	% change on Dec 29th 2006 in local currency	% change on Dec 29th 2006 in $ terms
United States (DJIA)	13,968.1	+0.6	+12.1	+12.1
United States (S&P 500)	1,539.6	+0.9	+8.6	+8.6
United States (NAScomp)	2,729.4	+1.1	+13.0	+13.0
Japan (Nikkei 225)	17,199.9	+4.6	–0.2	+1.9
Japan (Topix)	1,664.0	+5.6	–1.0	+1.0
China (SSEA)	5,827.7	+4.0	+107.0	+115.3
China (SSEB, $ terms)	367.4	+2.8	+171.5	+182.3
Britain (FTSE 100)	6,535.2	+1.6	+5.1	+9.3
Canada (S&P TSX)	14,020.9	–0.1	+8.6	+26.8
Euro area (FTSE Euro 100)	1,390.9	+1.5	+8.8	+16.7
Euro area (DJ STOXX 50)	4,421.6	+1.3	+7.3	+15.1
Austria (ATX)	4,687.1	+3.4	+5.0	+12.6
Belgium (Bel 20)	4,379.7	+2.2	–0.2	+7.1
France (CAC 40)	5,806.2	+2.0	+4.8	+12.4
Germany (DAX)*	7,955.3	+1.9	+20.6	+29.4
Greece (Athex Comp)	5,147.8	+0.9	+17.2	+25.7
Italy (S&P/MIB)	40,423.0	+0.9	–2.4	+4.7
Netherlands (AEX)	540.5	+0.2	+9.1	+17.1
Spain (Madrid SE)	1,616.3	+1.4	+3.9	+11.5
Czech Republic (PX)	1,835.1	+0.5	+15.5	+23.7
Denmark (OMXCB)	482.0	+2.0	+13.7	+21.9
Hungary (BUX)	28,044.9	+0.7	+12.9	+20.9
Norway (OSEAX)	562.3	–1.5	+11.9	+28.3
Poland (WIG)	60,947.0	–0.5	+20.9	+31.7
Russia (RTS, $ terms)	2,093.0	+2.1	+3.2	+8.9
Sweden (Aff.Gen)	386.9	+3.4	+5.9	+11.5
Switzerland (SMI)	9,088.7	+2.6	+3.4	+7.2
Turkey (ISE)	54,164.9	–0.1	+38.5	+63.3
Australia (All Ord.)	6,665.4	+2.7	+18.1	+32.1
Hong Kong (Hang Seng)	27,479.9	+4.0	+37.6	+38.0
India (BSE)	17,847.0	+5.5	+29.4	+44.8
Indonesia (JSX)	2,451.6	+3.8	+35.8	+33.8
Malaysia (KLSE)	1,367.0	+3.5	+24.7	+29.0
Pakistan (KSE)	14,045.2	+5.8	+39.9	+40.3
Singapore (STI)	3,754.6	+2.9	+25.7	+30.4
South Korea (KOSPI)	2,014.1	+4.9	+40.4	+42.9
Taiwan (TWI)	9,700.1	+4.8	+24.0	+24.0
Thailand (SET)	850.6	+0.7	+25.1	+32.1
Argentina (MERV)	2,254.1	+3.5	+7.8	+5.0
Brazil (BVSP)	60,098.0	+0.6	+35.1	+58.4
Chile (IGPA)	14,804.2	+3.1	+19.6	+26.1
Colombia (IGBC)	10,561.9	+1.4	–5.4	+5.3
Mexico (IPC)	31,178.8	+2.9	+17.9	+17.5
Venezuela (IBC)	37,517.7	+3.6	–28.2	+11.8
Egypt (Hermes)	76,926.9	+2.4	+25.5	+28.6
Israel (TA-100)	1,127.7	+2.9	+22.3	+28.6
Saudi Arabia (Tadawul)	7,765.2	–2.1	–2.1	–1.9
South Africa (JSE AS)	30,730.1	+3.1	+23.3	+26.3
Europe (FTSEurofirst 300)	1,571.0	+2.0	+5.9	+13.6
World, dev'd (MSCI)	1,647.7	+1.9	+11.1	+11.1
Emerging markets (MSCI)	1,233.4	+4.4	+35.1	+35.1
World, all (MSCI)	416.1	+2.2	+13.1	+13.1
World bonds (Citigroup)	698.6	+0.3	+6.1	+6.1
EMBI+ (JPMorgan)	424.5	+0.6	+4.2	+4.2
Hedge funds (HFRX)	1,330.8	+0.7	+4.3	+4.3
Volatility, US (VIX)	18.8	17.6	11.6	(levels)
CDSs, Eur (iTRAXX)†	35.9	+1.9	+54.0	+65.2
CDSs, N Am (CDX)†	57.6	–1.0	+72.2	+72.2
Carbon trading (EU ETS) €‡	21.7	+1.6	+18.9	+27.6

*Total return index. †Credit-default swap spreads, basis points.

Sources: National statistics offices, central banks and stock exchanges; Thomson Datastream; Reuters; WM/Reuters; JPMorgan Chase; Bank Leumi le-Israel; CBOE; CME; Danske Bank; EEX; HKMA; Markit; Standard Bank

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Doing business

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Singapore retained its ranking as the easiest place to do business in the World Bank's “Doing Business 2008” report, the fifth in an annual series. The rankings are based on ten quantitative measures of the regulatory environment for private firms. Egypt showed the biggest improvement compared with the last survey, advancing in five of the areas covered. A business can spring to life more quickly there than in Italy. Many of the countries making the greatest strides are in eastern Europe and the former Soviet Union. Ghana, Colombia, Saudi Arabia, Kenya and China are also among the top ten reformers. Congo, where it takes 155 days to get a business up and running, is the lowest ranked country in the survey.

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